

CA24N
CC 800
- 70761



DEPARTMENT OF FINANCIAL AND COMMERCIAL AFFAIRS

commissions and committees of enquiry

REPORT OF
THE MINISTER'S COMMITTEE ON FRANCHISING

July, 1971



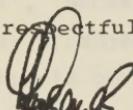
June 1st, 1971

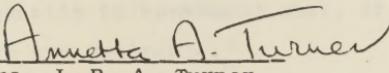
The Honourable Arthur Wishart, Q.C., M.P.P.,
Minister of Financial and Consumer Affairs.
Parliament Buildings,
Toronto 2, Ontario

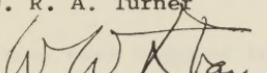
Dear Sir:

We now submit the final report of the
Minister's Committee on Franchises dealing with referral
sales, multi-level or pyramid sales, and franchises.

Yours respectfully,


S. G. M. Grange, Q.C.,
Chairman


Annetta A. Turner
Mrs. J. R. A. Turner


Watson W. Evans, C.A.

REPORT OF THE MINISTER'S COMMITTEE ON
REFERRAL SALES, MULTI-LEVEL SALES AND
FRANCHISES

INTRODUCTION

This Committee was formed by The Honourable Bert Lawrence, M.C., Q.C., in August of 1970, and was continued by The Honourable Arthur Wishart, Q.C., Ministers of Financial and Commercial Affairs, to review and report upon referral, pyramiding or multi-level sales practices, and franchises. The precise terms of reference are as follows:

"To review and report upon what are commonly described as 'referral', 'pyramiding' or 'multi-level' sales practices, arrangements and franchises, and to consider all aspects of the relationship of franchisors and franchisees and the implications of these arrangements to the consumer and the investor, and generally to recommend what, if any, changes in the law are desirable."

Since our appointment, we have been engaged in these enquiries with the most able assistance of our Counsel and Research Director, Professor W. A. W. Neilson of Osgoode Hall Law School, York University, and our Secretary, Mrs. D. A. Staff, Economist for the Department. We have now reached our conclusions and are ready to submit our report.

THE UNIVERSITY OF TORONTO LIBRARY
2010 RELEASE UNDER THE LIBERTY OF INFORMATION ACT

UNIVERSITY OF TORONTO LIBRARY

UNIVERSITY OF TORONTO LIBRARY
2010 RELEASE UNDER THE LIBERTY OF INFORMATION ACT
UNIVERSITY OF TORONTO LIBRARY
2010 RELEASE UNDER THE LIBERTY OF INFORMATION ACT
UNIVERSITY OF TORONTO LIBRARY
2010 RELEASE UNDER THE LIBERTY OF INFORMATION ACT
UNIVERSITY OF TORONTO LIBRARY
2010 RELEASE UNDER THE LIBERTY OF INFORMATION ACT

Digitized by the Internet Archive
in 2022 with funding from
University of Toronto

INDEX

| | <u>Page</u> |
|--|-------------|
| INTRODUCTION | 1 |
| CONDUCT OF THE INQUIRY | 2 |
| Division between subjects | 2 |
| Material | 2 |
| Hearings | 3 |
| Interim Reports | 4 |
| REFERRAL SALES | 5 |
| Complaints and Evils of the System | 5 |
| (i) Inflated price | 5 |
| (ii) Misrepresentation by salesmen | 6 |
| (iii) Irresponsibility of the principal seller | 7 |
| Mathematics | 7 |
| Solutions | 8 |
| (i) Abolition | 8 |
| (ii) Education | 12 |
| (iii) Control and Recommendations | 13 |
| MULTI-LEVEL OR PYRAMID SALES | 21 |
| Operation of the schemes | 21 |
| Unacceptable characteristics | 22 |
| (i) Sale of distributorships | 22 |
| (ii) Lack of training | 22 |
| (iii) Promotion | 23 |
| (iv) Contractual inequality | 23 |
| (v) Fees | 24 |
| (vi) Mathematics | 24 |
| Solutions | 25 |
| (i) Criminal Code, section 179(1)(e) | 25 |
| (ii) The Securities Act | 26 |
| (iii) Recommendations | 26 |

| | <u>Page</u> |
|---|-------------|
| FRANCHISES | 36 |
| Definition | 36 |
| General Problems | 38 |
| (i) Contractual inequality and collective bargaining | 38 |
| (ii) Termination and assign- ment | 40 |
| (iii) Coercion and secret profits | 41 |
| (iv) Competition and discrimination | 42 |
| (v) Inducement and advertising | 43 |
| (vi) Financial irresponsibility of franchisors | 43 |
| Particular Problems | 44 |
| (i) The oil industry | 44 |
| (ii) The automobile industry | 46 |
| (iii) The fast food industry | 48 |
| (iv) Small investor franchises | 48 |
| (v) The Becker problem | 49 |
| Legislative approach | 52 |
| (i) Legislation or not? | 52 |
| (ii) Generic or single industry | 52 |
| (iii) Contractual or equitable | 53 |
| (iv) Administrative control | 55 |
| (v) Recommendations | 56 |
| SUMMARY OF RECOMMENDATIONS | 66 |
| Referral sales | 66 |
| Multi-level or pyramid sales | 66 |
| Franchises | 67 |
| General | 68 |
| APPENDICES | 69 |

CONDUCT OF THE INQUIRY

Division between subjects

For the convenience of the witnesses and ourselves, we endeavoured to keep the study of the three subjects separate wherever possible, and in the actual public and private hearings, we heard first, witnesses dealing with referrals or multi-level sales, and latterly witnesses dealing with franchises, but it must be emphasised that the arrangement was one of convenience only. In many respects, the subjects are inter-related, and, indeed, in many respects all three subjects are related to the larger subjects of consumer sales and investments generally. While we deal only with the three subjects and divide them into somewhat arbitrary categories, we fully appreciate that the Minister and his advisors may wish to relate the subjects more closely and may wish to apply some of our recommendations to larger fields.

One of the difficulties in this fragmentary approach, however, is that we have occasionally reached slightly different recommendations upon the different subject matters, when we could just as conveniently have made them identical. We have attempted to co-ordinate these recommendations to some degree, and in our Summary of Recommendations, we have listed those which are common to two or more fields. We hope, therefore, that this difficulty has been partly overcome.

Material

Professor Neilson supplied us voluminously with material on the subjects as follows:

Referral Sales:

- (a) the results of interviews with a wide range

of officials in business, government and consumer groups in Canada and the United States.

- (b) Provincial, Federal and United States legislation.
- (c) Pertinent judicial and administrative rulings in Canada and the United States.
- (d) A comprehensive survey of the structure and procedures of the referral selling industry.

Multi-level sales:

- (a) Canadian and United States proceedings against various companies in the field.
- (b) Informative releases from Canadian and U.S. Departments of government dealing with consumer affairs and from independent organizations.
- (c) Literature from some of the companies involved directed to their salesmen and recruitment officers

Franchises:

- (a) Articles and texts on franchising.
- (b) U.S. and other foreign legislation and proceedings of legislative and administrative hearings.
- (c) Canadian studies both public and private and both general and particular
- (d) The results of questionnaires sent to selected franchisors and franchisees in Ontario.

Hearings

We decided to seek such further assistance as we could from the public, and accordingly, advertised in September for written communications and oral testimony in relation to referrals and multi-level sales, and in December for the same with reference to franchises. We are listing in the appendices the briefs and other communications received and the persons making oral reports at the public hearings. Because of the delicacy

of the position of some of the potential witnesses, we decided to hold private hearings as well, and the witness himself would generally determine whether he would be heard publicly or privately. A list of the dates upon which private hearings were heard is also to be found in the appendices. We do not, of course, wish to reveal the names of the witnesses because in many instances it might jeopardize the position of that witness, but it is remarkable how often the private hearings were resorted to by large corporations or organizations enjoying complete security in their business operations. We can only assume that the fear of media distortion or publicity in general militates against participation in open hearings.

Interim Reports

After the public hearings in October and the private hearings in and about that period, we felt that we were in a position to make interim reports, and accordingly an interim report on referral sales, signed December 8th, 1970, and one on multi-level sales, signed January 5th, 1971, were submitted to the Minister. The substance of these reports is incorporated in this final report. Some minor changes have been made in the recommendations of the interim reports, and some co-ordination has been made in the administrative controls to bring them into line and sympathy with the recommendations in the part of this report dealing with franchises.

REFERRAL SALES

Complaints and Evils of the System

The referral sales system has been given many definitions but essentially it is a system whereby the seller enlists the aid of the buyer in effecting further sales of the product, and rewards or promises to reward the purchaser for that assistance. In most cases the assistance takes the form of the purchaser supplying to the seller the names of prospective purchasers and the seller either paying for those names or paying a larger amount in the event of a sale being effected to the prospective purchasers. The sellers have described the system as no more than the legitimate extension of normal marketing procedures. We believe, however, that any economic benefit accruing to the market by permitting the continued, unfettered conduct of this method of sale is outweighed by the harm suffered by many buyers in the course of it.

The complaints we received relating directly to the system can be classified under the following headings:

- (i) Inflated price
- (ii) Misrepresentation by salesmen
- (iii) Irresponsibility of the principal seller.

Dealing with these complaints in order, the following would appear to be the relevant facts:

(i) Inflated price

While it is perhaps difficult to compare the value of an article that is not generally marketed with others of the same general standard, it became abundantly clear that

most of the articles marketed under the referral sales systems were vastly over-priced. This is particularly unfortunate for the purchaser because, as will be seen, the success of the referral system is not very wide-spread, and the chances of reducing the cost by means of referrals is slender.

(ii) Misrepresentation by salesmen

There appears to be inherent in the system a temptation to very high pressure salesmanship and, indeed, to misrepresentation of the nature of the contracts being entered into by the purchaser. There are, of course, some honest, responsible salesmen involved in these schemes but it is to be remembered that they are always on commission and that where there is a referral element promising some chance of reward to the purchaser, it would take a very scrupulous salesman not to exaggerate the chances of that reward being greater than, indeed, experience has proved. There were many instances of salesmen actually assuring the purchaser that the referral system would pay completely for the article purchased, and obtaining the purchaser's signature to a contract which in the usual form negatived any association or dependence of the referral system upon the contract of sale. It was generally not until the finance company's request for payment came to hand that many of the purchasers discovered firstly that they had contracted for the purchase of the article regardless of the success of the referral scheme and secondly that the referral scheme was unlikely to succeed. We might point out

that financing is encouraged by sellers apparently because it often represents an extra source of revenue to them in that they receive some consideration for each contract financed. It is, perhaps, a reflection upon the whole referral system that most purchasers sooner or later come to regret their bargain.

(iii) Irresponsibility of the principal seller

Generally speaking, the manufacturers or local distributors of the articles sold so arrange their affairs that the salesmen are employed by an independent company. The articles are then sold to the selling company and no contractual relationship exists between the original distributor and the purchaser. Added to this, there have been complaints that the salesmen are not following up referral leads, and even complaints that the promises of payments for successful referrals are not honoured. We have, then, the situation where the purchaser is bound by a contract to pay and the real (although not legal) seller has no enforceable responsibility to follow up referrals or even to maintain warranties and repairs, etc.

Mathematics

It is obvious that no referral scheme can operate fully as predicted by many of the sellers, and as contemplated by many of the purchasers. Where a purchaser hopes to recover his investment by a number of referrals, each of these referees will require a similar number of referrals to recover his investment in turn. It takes very little imagination to realise that it will take very few stages of this geometric progression before

many millions of people will be required to participate in the scheme in order to make it a success. Practically speaking, however, the problem may not be as severe as the mathematics would indicate, and this is quite probably due to the fact that the referral scheme seldom works as promised or contemplated; experience seems to show that on an average, not more than one, or at the most two, referrals are satisfactorily concluded for each purchaser.

Solutions

We have sought assistance in proposing the legislative and other remedies for the evils of the system from many sources. We have had the advantage of reading the legislative proposals and enactments of other jurisdictions and we have put questions to the representatives of various companies who have appeared before us, and also to some of the purchasers who are complaining of the purchases made. Short of leaving the matter to the present remedies given at law (which might produce, and indeed have in many instances produced, a just result - but which in our view are, generally speaking, inadequate) there appear to be three different solutions as follows:

- (i) Abolition
- (ii) Education
- (iii) Control.

(i) Abolition

As to the first proposal The Consumers Association of Canada (Ontario branch) strongly recommended any action that would result in the disappearance of the referral system. There has been an attempt at abolishing the system in British Columbia and to a certain lesser extent in some of the other provinces,

and also completely in some of the states of the United States. In the State of New York, on the other hand, the legislature there has attempted to control the practice rather than outlaw it. Where the object is abolition, the approach is sometimes to adopt the simple device of rendering a contract in which there is a referral element unenforceable, and thus give the purchaser the right to retain the goods without payment. Specifically, the British Columbia legislation reads as follows:

Section 5A, B.C. Consumer Protection Act

"An executory contract is not binding on the buyer if with respect thereto the seller gives, or offers to give a rebate or discount to the buyer in consideration of his giving the seller the names of prospective purchasers, or otherwise aiding the seller in making a sale to another person, if the earning of the rebate, discount or other value is contingent upon the occurrence of an event subsequent to the time the buyer agrees to buy."

Even if we were disposed to the total abolition of referral sales, we would hesitate to recommend the adoption of the B.C. legislation for the following reasons:

(a) We do not believe that the non-enforcement should be related only to executory contracts. We see no reason why an executed contract could not be rescinded and the moneys returned to the buyer.

(b) We think that the legislation leaves a very glaring loop-hole in that the sellers can and do separate the selling end of the transaction from the referral end of the transaction, usually by the simple device of incorporating them in separate documents. We believe that

any legislation involving abolition, to be effective at all, would have to ensure that any transaction containing any referral element, be it coincidental with, before or after the sale, should be rendered void.

(c) Leases are being used with increasing frequency in consumer transactions and we see no reason why any legislation should not cover leases as well as sales.

The Province of Saskatchewan has attempted to effect the same purpose by the licensing approach, and their statute reads as follows:

"The licensee shall not give or offer to give directly or indirectly, any gift, premium, prize or other benefit of any kind whatsoever to a purchaser or prospective purchaser for services in furthering the sale to another person of any goods or services if such gift, premium, prize or other benefit is contingent on a sale being made to such other person."

In our view this legislation is even less effective because the contingency depends upon a "sale being made" and that eliminates all protection from the kind of referral that does not involve a sale but merely the delivery of names to the seller. We believe that legislation in the following form would be appropriate and effective:

"A contract is not binding upon the buyer or the lessee if with respect thereto the seller or lessor gives or offers to give any gift, premium, prize, rebate, discount or other value or benefit of any kind whatsoever to the purchaser or lessee for services in furthering the sale or lease, or potential

sale or lease to another person, whether the said gift or other benefit be coincidental with the sale or lease or otherwise, and whether the same be part of the same transaction or otherwise.

"The purchaser or lessee may at his option rescind the contract and receive back any moneys paid by him in furtherance of the transaction upon surrendering the goods received by him pursuant thereto."

In any event, we have considered the possibility of abolition and have reluctantly decided against making any such recommendation because we feel that at this time there is a possibility that a legitimate enterprise could be run under the referral system if proper controls were established. We believe that we would be failing in our duty if we took the approach of outright abolition, which, from a legislative standpoint, is easier to set forth, and thus deprive certain businesses of engaging in practices to which they are well adapted and which they try to conduct honestly. We believe that, generally speaking, the referral system works to the detriment of the purchaser, and that almost invariably the price for the article sold is greater than that for a similar article sold in the ordinary market. But we also believe that in some instances a purchaser can, by successful referrals, substantially reduce the purchase price and thus be able to purchase an article he would not otherwise be able to enjoy. Consequently, for the benefit of the somewhat rare purchaser and the perhaps even rarer seller, we are reluctant to outlaw the practice:

(ii) Education

Many witnesses before us and many of the briefs received, advocated the education principle, and chief among these were the Consumers Association of Canada (Ontario Branch) the Better Business Bureaux, and in one case, a Professor from the University of Toronto. It is interesting to note that the Better Business Bureau of Toronto recommended apart from education, that no action be taken on referral sales, and the General Manager of the Better Business Bureau of Mainland B.C. took pride in the fact that the British Columbia legislation had largely eliminated all referral sales in that province. Everyone believed in education and it is difficult to deny the theoretical advantage of massive propaganda against the evils of the system. However, it is our view that generally speaking such educational efforts have been ineffective and have failed to reach the people most in need of education.

Even those who can read do not bother to do so, and all the purchasers seem to have accepted the word of the salesman, even when it was flatly contradicted by the words of the document they signed. There is no question here of any inequality of contract in any legal sense, but from a practical standpoint a purchaser seems to have little chance against the wiles of the eloquent salesman. Enlightenment comes eventually, but too late for recission.

(iii) Control and recommendations

We are of the opinion that referral selling can be maintained, if rigidly controlled, and to effect such control we recommend the following:

1. There should be enacted a new part of the Consumer Protection Act entitled "Referral Sales and Leases".
2. This part should be made to apply to any sale or lease whereby any reward is offered for supplying names or other services by a purchaser or lessee, whether or not such reward should be conditional upon a sale or lease and whether or not the offer of a reward should be coincidental with the sale or lease, and whether the transaction takes place in the home of the purchaser or lessee or the business premises of the seller or lessor or otherwise. For convenience we refer hereafter to sale and seller and purchaser, but we mean all recommendations to have reference to a lease transaction as well. The problem of leasing is perhaps not immediate, but there have been some instances, and we can foresee it looming larger, not only in referrals but also in multi-level and franchise matters, as a device to subvert the legislation. It is to be hoped that the legislation as drafted, by covering leases as well as sales, will defeat that object. We also recommend that this part apply notwithstanding Regulation 2 of the Consumer Protection Act, which, in our view, appears

to exempt from the provisions of the Act the original distributor of the goods or services and any person down the line from him who may purchase and sell the goods. In other words, we think that the exemption in Regulation 2(1) must be radically amended, or it must be made not to apply to the section dealing with referral sales.

3. We propose that the original Ontario distributor be made responsible for the actions of the "independent contractor" who performs the actual sales operation and that both be made responsible for the contractual obligations imposed upon the seller by the legislation. For convenience we refer to "sellers" hereafter but mean both sellers and original Ontario distributors.
4. We propose that no seller should be entitled to indulge in any referral sale without having his form of contract approved by the Registrar or some other official. No doubt the organization will be in line with Part I of The Consumer Protection Act, as amended in the Statutes of Ontario (1968-9). Admittedly the contract terms will be fairly rigidly set forth below, but we, nevertheless, think it would be of substantial value to the consumer to have some check upon these sellers prior to their institution of business. Naturally, we believe that the refusal of the Registrar to approve a contract should be subject to appeal, as should many of the other provisions hereinbefore and hereinafter set forth, but the

advantage of having approval before the institution of business is that it may well present any disreputable seller from getting started at all.

5. We propose also that the bonding of sellers dealing in referral sales should be substantially modified and extended. Regulation 6 of The Consumer Protection Act provides for certain bonding regulations. It is our proposal that the activities of referral sellers be considerably limited by requiring substantial bonds and requiring the forfeiture of these bonds and the automatic cancellation of the license of the seller if there is a breach of the legislation or the regulations. We propose this not only for ready control of the referral sellers, but also for the protection of the purchasers in the event of a defaulting or absconding seller.
6. We propose that all contracts containing a referral element shall,
 - (a) be entitled for ease of reference and for warning to finance companies, etc. "Referral Sale or Lease Contract";
 - (b) contain the referral element as a promise of the seller;
 - (c) require the seller diligently to perform the promise with respect to the referral element;

(d) require all services and warranties given by the seller (and by reason of paragraph 2 above, also by the original distributor) to be set forth as an obligation of the seller. (This admittedly does not answer the larger problem of what these warranties should be, a problem common to all sales);

(e) require that all the terms in this paragraph and of paragraphs 7 and 9 below, be included in the contract in distinctive block letters.

7. We propose that the purchaser be entitled to rescind the contract at any time within seven days of the execution of the contract and at any time if the provisions of 6 above are not followed. In the event of such recission,

(a) the purchaser will be required to return the goods bought;

(b) the seller will be required to return the money (it is to be noted that by a combination of this paragraph and paragraph 6(e) above, any assignee of the contract will also be subject to suffer the recission - this would appear to be in line, also, with the philosophy of section 27a of the proposed amendment to The Consumer Protection Act).

8. We propose that the Registrar or some other official of the Department be entitled to cancel or suspend licences of sellers whenever,

(a) there is a failure to abide by the provisions of paragraph 6 above, e.g. failing to state the compulsory terms in the contract;

(b) there is, in the opinion of the Registrar (subject to appeal) a deception by the seller as to the true intent of the contract, or as to the terms thereof;

(c) there is a failure on the part of the seller to carry out the services and warranties required to be performed by him in the contract. (Because of recent amendments to the Act it may be that the power of the Registrar will devolve upon The Commercial Registration Appeal Tribunal).

9. We propose that the remedy of the seller for non-payment (and as will be seen, such remedy will apply also to the purchaser of the sales contract) shall be limited to the seizure of the goods sold and no remedy will be available to collect the balance of the purchase price. There should be an exception to this limitation and that is, if the goods are not returned in reasonable condition having regard to the period and circumstances of use, the normal remedy should be available to the seller or his assignee. This is, quite frankly, a most drastic remedy, giving the buyer a right to limit his loss to the amount already paid for any reason whatever, but it is chiefly intended to control sales at inflated prices. When a purchaser discovers that he has been badly cheated on the price he should not be required to go on paying.

It is our view that such a provision would have a salutary effect not only in correcting injustices to the buyer but also in inhibiting sales at inflated prices. This provision, of course, will not assist any person who pays cash for his purchase, but he may have a remedy otherwise, e.g. rescission under paragraph 7 above. We also realize that if the transaction is conducted in such a way that the finance company makes a loan of the full purchase price to the purchaser rather than purchasing the contract from the seller, this clause will little avail the purchaser. It might be possible to cover this situation (as is attempted in section 189(3) of the recently amended Bills of Exchange Act) but in our view it would be very difficult to distinguish between a legitimate loan and one which was designed purely to enable the finance company to bring action for the whole purchase price.

10. We propose that there be a prohibition of the "cut-off clause" which, notwithstanding the amendment to the Bills of Exchange Act respecting "consumer notes", may enable the purchaser of the contract (the finance company) to avoid any responsibility imposed upon the seller by the proposed legislation. It is possible that such protection is given in the Personal Property Security Act of Ontario by section 16, but this Act has not yet come into effect. Obviously this is a problem of wider application than merely referral sales, and at the time of the preparation of this

final report, an aspect of the subject is before the Legislature in Bill 47 of 1971.

We are of the firm belief that the proposals here made for control are a package in the sense that except for necessary modifications to suit the legislative problem, all should be included in any amendments to the Act. As we stated before, we reluctantly decided against outright abolition of referral sales, and we still entertain some doubts that even the strict proposals here made will resolve the problem. We do feel, however, that unless all, or substantially all of the proposals are enacted, it would be better to go back to outright prohibition. We also realize that there may be financial and administrative problems which will make our proposals impractical. Certainly we realize that these proposals require a good deal of refinement and we would be happy to assist any person more qualified than we are in the drafting of the legislation. We have already discussed some of these proposals with members of the Department, but once again, we would be most happy to consult further with them and consider any modification of these recommendations.

There are just two further proposals that we should refer to and these are ones that we think have merit but have not recommended, either because of uncertainty of their effect or because of the apparent administrative difficulty involved. The first is some provision limiting the number of referrals that can be made in any given transaction. On the one hand it can be said that such limit would make it

readily apparent to the purchaser that the whole of the purchase price could not be defrayed in such a manner; on the other hand, it might merely enable the seller to limit the profits of a particularly industrious purchaser. The second proposal was the licensing of individual salesmen. We would have thought that this would give the Department an additional and an important control over the whole system, but we are informed that the idea is impractical because of the number of salesmen and the nature of their entry and departure from the business.

MULTI-LEVEL OR PYRAMID SALES

Operation of the Schemes

The multi-level or pyramid sale system has had many definitions, both by its friends and its detractors but essentially it is a system of marketing goods or services wherein members of the public are recruited to different levels of distribution depending upon the amount of their investment. The smallest investor generally sells the product to the public, and those up the line from him profit from his efforts and from his investments in attaining a higher position in the pyramid.

Before dealing with the complaints and evils of a scheme such as that above described, we should point out that there are in operation, schemes of a multi-level or pyramid nature which, at least so far as their literature divulges, purport to be based primarily upon the sale of the product and to limit investment to those who have proven ability to sell it. They further undertake the training of all salesmen and investors thoroughly, and reward investors solely for their success and the success of those they have brought into the scheme in marketing the product. These schemes also purport to limit the distributors by area and to permit unsuccessful investors and salesmen an opportunity to obtain a refund on the investment should it prove unsuccessful. It is not these schemes of which we complain, but it is our experience that much more common are the schemes containing most unsatisfactory characteristics which we describe in the following paragraphs.

Unacceptable characteristics

(i) Sale of distributorships

The emphasis in such schemes is upon the sale of distributorships, not upon the sale of the product. This is not too surprising because the schemes are so arranged that the profits from the sale of distributorships are vastly greater than the profits involved in the commission for sale of the products and there is therefore a natural tendency to emphasize the sale of the one over the other. In some instances, indeed, there is no product at all, and all that is being sold is an interest in a product as yet unborn. For example, it might be a right to a discount at a promised department store, or in a number of existing stores not yet committed to the scheme. The perils in such instances are obvious. The distributorships may be sold and prove valueless even in the hands of dedicated salesmen.

(ii) Lack of training

In these schemes the contract of investment requires the stocking by an investor of large supplies of the product and even assuming that the product is immediately marketable, there appears to be little concern with the ability of the investor to market it. The advertisements for investments in some cases, indeed, make much of the fact that no previous training is required. Most of the promoters proceed to provide some form of training, but it is not, in our view, generally adequate, and often involves additional fees or other financial outlay on the part of the investor. The result of these factors is, of course, that the investor

finds himself with large quantities of the product on hand, with no right to return it to the promoter, or only at prohibitively high discount, and with no ability to dispose of it satisfactorily. Moreover, little regard seems to be given by the promoter to the territory to be canvassed by the investors or the possible saturation of the market.

(iii) Promotion

There is in such schemes, also, perhaps as a necessary corollary, a tendency to promote the sale of these distributorships with almost evangelical fervour combined with a disinclination to disclose very relevant information regarding the numbers and success of other investors in the scheme. The common practice in recruiting investors is to obtain their attendance at what is sometimes termed "an opportunity meeting" at which prospective investors are presented with a picture of the merits of the scheme in the most glowing terms by some very persuasive and possibly convinced people. Possibly, also, the picture they present is true for those who present it because, for some, these schemes are indeed profitable, but for the vast majority who enter them, the glow is quickly extinguished, but not until after the contract has been signed and the investment has been made. It is essentially what these investors get in return for their investments that creates the problem.

(iv) Contractual inequality

Following upon the recruitment, a contract is entered into between the distributor/recruiter

and the recruit which reflects the persuasiveness of the former and the gullibility of the latter. These contracts require the investor to purchase large quantities of the product, to involve himself in further fees, and leave him with little redress if the scheme does not work out as well as the prediction.

(v) Fees

The use of the investment also causes us some concern. Generally speaking, the investment does not go to the development of the product but goes to the person responsible for bringing in the investor and to the promoters of the company. The investment, in short, is the price at which rank in the organization is bought, and it is easy to see that a scheme based upon that principle can hardly be conducive to an orderly and successful marketing of consumer goods.

(vi) Mathematics

The mathematical difficulties involved in these schemes are much more readily apparent than in the referral schemes, and while the schemes emphasize the potential rewards from the recruitment of others and further recruitment ad infinitum, there appears to be neither discussion of nor realization of the mathematical problems. For these schemes to work at all in accordance with the predictions given at the opportunity meetings, each investor must obtain some other investors to come in at his level or at some lower level. Obviously, there comes a time when this is physically impossible, and obviously also, a greater benefit accrues to those who are in on the scheme at the beginning.

In summary, therefore, the evils of the scheme relate to, (a) emphasis upon the sale of distributorships rather than the sale of the product; (b) over-enthusiastic promotion and non-disclosure by promoters; (c) unfair contracts; (d) disposition of investment; and (e) mathematics. With these evils in mind we propose solutions as follows:

Solutions

We did not have here the fundamental problem of abolition or control that we faced in the referral situation. No-one seriously suggested that all multi-level schemes should be done away with, and no-one seriously suggested that legislation was not needed. Our problem is the nature and form of that legislation. As a preliminary, however, we had to consider existing legislation in or affecting this province, and whether or not it was sufficient. Particularly we were concerned with The Criminal Code, section 179(1)(e) and The Securities Act.

(i) The Criminal Code

The Criminal Code section which was enacted originally to deal with chain letter schemes has been applied in Quebec successfully to obtain convictions against some of the multi-level operators. We have some doubt of the applicability of that section to any of the schemes, and have considerable doubt that it could apply to all of the schemes. In any event, it was obviously outside our terms of reference, and apparently the responsible officials in Ontario have decided that the Code is an inappropriate vehicle to resolve the problem.

(ii) The Securities Act

The Securities Act has been applied in British Columbia and Alberta and under similar laws in some of the United States to control some of these operations. We express no opinion as to whether the investments under a multi-level scheme are always or sometimes investments within the meaning of The Securities Act, but it is probably wise in any event to have distinctive legislation because multi-level schemes are quite different from most other investments and may well require legislation specifically designed to deal with them.

(iii) Recommendations

Assuming, therefore, the non-applicability of The Securities Act and The Criminal Code, we propose the following to resolve the problems outlined above:

1. There shall be enacted legislation dealing with multi-level schemes. This legislation is in many ways similar to the franchise legislation that we are recommending. It is not, strictly speaking, what we consider consumer legislation. It has many similarities to securities and companies legislation, and might conceivably be brought under the Securities Commission or under the Companies Branch. It might also be brought under the Consumer Protection Division with a separate Act of its own, but we incline to the view that the problems involved are too large and too varied for the Consumer Protection Division, and should be operated separately.

As will be seen, such operation will require the appointment of a "Registrar", and we cannot stress too much the importance of the man who will undertake the duties of the Registrar. If the man deals only with multi-level schemes, he will, nevertheless, be concerned with the operation of some very complicated, sophisticated schemes, and some very astute, experienced operators. If he is also to deal in franchises, he will be required to deal with some of the largest corporations in the country, and with many extremely varied types of franchise relationships. It is our firm belief that there can be no effective control of either branch unless there is not only a very dedicated, but also a very able man at the administrative helm.

2. There should be a definition of "multi-level schemes", "multi-level promoters" and "multi-level investors". These definitions, particularly that of the schemes, are of vital importance, and we would be happy to assist the draftsmen of the legislation in formulating them so as to ensure that the legislation effectively controls the schemes depicted above and does not unnecessarily hinder the operation of other businesses. The essential distinguishing feature of the scheme is that the investment brings with it in return a right to recruit other investors. There is a dearth of legislation on the subject matter, but perhaps the definition of "chain distributor scheme" in the Wisconsin Administrative Code, which is as

follows, may be of assistance:

"'Chain Distributor Scheme' is a sales device whereby a person, upon a condition that he make an investment, is granted a license or right to recruit for profit one or more additional persons who also are granted such license or right upon condition of making an investment, and may further perpetuate the chain of persons who are granted such license or right upon such condition. A limitation as to the number of persons who may participate, or the presence of additional conditions affecting eligibility for the above license or right to recruit or the receipt of profits therefrom, does not change the identity of the scheme as a chain distributor scheme."

The new Alberta legislation (to which reference will be made below in relation to franchises) defines "pyramid sales franchise" as,

"any scheme.....whereby a participant..... is required or receives the right to recruit one or more persons as participants who are subject to a similar requirement or who obtain a similar right, and...(receives a benefit therefor)....."

We cannot leave the subject without confessing that the problem of definition will be the most difficult task of the draftsman of the legislation. It is obviously essential to include all schemes having the recruitment for gain element, but equally important to exclude ordinary marketing schemes where the rewards are dependent upon the sale of the product and not upon the recruitment of other sellers.

3. In order to prevent these schemes from getting started without a thorough examination to determine whether they are feasible and proper, we have adopted the approach of requiring the filing of an outline of the scheme or a prospectus with some official or body for examination and approval. For purposes of convenience only we have referred to the filing of the prospectus with the 'Registrar', but we fully understand that from an administrative view-point it may well be desirable to impose that obligation upon some other official or some other body. Wherever hereafter the word "Registrar" is used, it is to be understood that the eventual legislation may well substitute some other word.

No multi-level scheme shall be permitted to operate or to advertise for investors until there is filed with and accepted by the Registrar an outline of the scheme or prospectus, which outline shall include,

- (a) the names and addresses of the promoters and of the principals (whether persons or corporations), affiliates and subsidiaries of the promoter, and the relationship of such affiliates and subsidiaries to the promoters, together with such information concerning the identity and business experience of such persons or corporations as the Registrar may require or the Regulations prescribe;
- (b) the nature of the product, its source of supply and all provisions for warranties to be granted to the ultimate consumers and the facilities for implementing these warranties;

- (c) the numbers and levels of distributorships, including the number of distributorships in each level, the investments required to attain such levels, the control of locations and areas assigned to investors, the inventory which is to be supplied to investors for any particular investment, the terms upon which further inventory is to be made available and, where the promoter is dealing in a variety of products, information on the distribution of the various products to investors in return for their investment;
- (d) the provision for training of investors and salesmen;
- (e) the disposal of the funds invested, including all fees paid to members of the scheme;
- (f) all additional charges or fees to be imposed upon an investor after investment, including further purchase obligations;
- (g) the form of contract intended between the investor and the promoter;
- (h) such other information relating to the scheme as the Registrar may require for the proper evaluation of the scheme.

In addition to all of these requirements, some consideration might be given to requiring the much more detailed information that we have recommended to be filed with relation to franchisors. See page 57 et seq infra.

4. The Registrar may upon receipt of the prospectus and the payment of an appropriate fee, accept the prospectus for filing or he may decline to accept it if, in his opinion,
 - (a) the prospectus contains any misleading fact or omission;

- (b) there is no immediate availability of the product for marketing;
- (c) there is inadequate provision for marketing of the product, protection of investors and purchasers and training of investors and salesmen;
- (d) where the promoter is dealing in a variety of products and there is not available to the investor upon reasonable terms all such products;
- (e) where there is not available to investors a ready access to further products when needed;
- (f) the outline does not provide for the delivery of product to the investor to a retail value of at least the amount of the investment;
- (g) if more than 10% of the investment is devoted to finders' fees or other benefits to other participants in the scheme;
- (h) if in the opinion of the Registrar, the proceeds from the investments that are to be paid into the treasury of the promoters, together with other resources of the promoters, are insufficient to render the scheme feasible, or enable the promoters to comply with obligations imposed under this Act.

5. There shall be filed with the Registrar all variations in the scheme as originally filed and approved prior to such variations coming into effect, and no such variations shall come into effect unless approved by the Registrar.

6. The Registrar shall be entitled at any time to call for, and there shall be filed annually with the application for renewal of approval of the scheme, the following:

- (a) an audited financial statement;

- (b) an affidavit setting forth any changes in the scheme since the last filing, or stating that no such changes exist;
- (c) a copy of the register of investors hereinafter referred to.

7. No promoter or investor shall enter into an agreement with a person by which such person would become an investor, unless the promoter or investor has delivered a copy of the prospectus (including a copy of the proposed contract) to a prospective investor, at least 48 hours before the execution of the agreement.

8. The contract of investment shall contain as a compulsory provision thereof, printed in distinctive block letters, a clause permitting the investor to return the product, or such portion thereof as has not been disposed of, and receive in return at least 75% of his total investment, or 75% of the appropriate portion thereof at any time within six months from his original investment in the scheme. There should be adequate provision to compel the immediate return of the investment by the promoter upon demand by the investor, but there should also be a right to the promoter for relief in the event that the investor is unable to return the product in merchantable condition considering all the circumstances. It should also be provided that if the contract does not contain the said term, the right to recission on the part of the investor will be absolute and permanent.

9. We have given a good deal of consideration to the problems involved in bonding to protect the investors and ensure the enforceability of the buy-back clause above. We understand that there are at present three deficiencies in the operation of the bonding system. The first is that there is delay in the forfeiture and realization upon the bond; the second is that the bond is generally inadequate; and the third is the unavailability generally of bonds. We believe that the mechanics of bonding are too difficult to be effective and we suggest instead, therefore, that the Registrar would be empowered to require that a proportion of all moneys invested in the scheme be held in escrow until sufficient moneys are available to implement the scheme satisfactorily. It may be that he will order all moneys held in escrow in some schemes, but in many of them there is an immediate delivery of goods and it would probably not be feasible to require an escrow of all the investments.
10. The promoters of every scheme shall be required to maintain a register of the names and addresses of all persons who have invested in the scheme. This register should be kept in the place of business of the promoter in Ontario and should define the territory allotted to each investor. The register should be open for inspection by the Registrar or by any investor or potential investor during business hours at any time without fee.

11. There should be provision for cancelling the right of the promoter to carry on the scheme, similar to section 6 of the amended Consumer Protection Act. It has been suggested that possibly the procedure under section 7 of the amended Consumer Protection Act would give too much time to the promoter to carry on a fraudulent scheme, and it may be that provision should be made in extreme cases for the tribunal to issue some sort of *ex parte* injunction at the request of the Registrar. A similar provision has been suggested for franchising and presumably the requirement in relation to both subject matters will be co-related.
12. There should be a right to the Registrar to enter upon the business premises of the promoter to make inspections to ensure the scheme is being operated in accordance with the approved prospectus, similar to section 25 of The Real Estate and Business Brokers Act as amended by chapter 105 of the Statutes of 1968-69.
13. There should be provision with respect to advertising similar to section 31 of the amended Consumer Protection Act. A somewhat similar provision is also recommended in relation to franchises.

We should like to emphasize that we consider paragraphs 4(f) and 8 essential to the elimination of the major present defect of these schemes. It is our view that so long as the promoter is permitted to accept an investment without giving a product in return, and without the right of the investor to return the product and receive back at least a major

part of his investment, the evil will persist. We also think that paragraph 4(g) is important, as the payment of fees for the recruitment of investors is an integral part of these schemes and the payment of large fees is the source of much of the evil found therein.

FRANCHISES

Definition

It became immediately apparent to us when we began our researches, and it has remained pressing throughout the hearings, that one of our most difficult problems is that of definition. The word "franchise" originally meant royal or public grant of rights or privileges, e.g. a right to operate a railway or a right to vote. The expansion of the word to relate to dealings between citizens is relatively new. It became obvious to us that the word had been used to describe the relationship between the parties in varying situations without too much concern as to whether the use was appropriate. Possibly this lack of concern arose naturally from a lack of legislation governing the relationship, but as soon as it became apparent that legislation was contemplated, the semantics of the problem became more interesting. Predictably those granting the privilege tended to deny the existence of a franchise relationship, and those in receipt of the grant tended to assert it.

In our view, a franchise is essentially the grant of a right to operate a business, which business involves the use of the grantor's trade mark or trade name, and some substantial control of the grantee's operation of the business by the grantor. Without the trade mark or trade name, there can be no franchise at all, and it is the element of control that distinguishes, in our view, a franchise from either a bare licence or an employment contract. In a bare licence there is little or no control, and in an employment contract, there is almost complete control.

Other jurisdictions have struggled with the definition. An example from the proposed Massachusetts Statute is as follows:

"Franchise" shall mean an oral or written agreement for a definite or indefinite period, in which a person grants to another person a licence to use a trade name, service mark or related characteristic, and in which there is a community of interest in the marketing of goods and services at wholesale, retail, leasing or otherwise".

The California Franchise Investment Act contains a definition as follows:

"Franchise" means a contract or agreement, either express or implied, whether oral or written, between two or more persons by which

- (a) the franchisee is granted the right to engage in the business of offering, selling or distributing goods or services under a marketing plan or system prescribed in substantial part by the franchisor; and
- (b) the operation of the franchisee's business pursuant to such plan or system is substantially associated with the franchisor's trade name, logotype advertising or other commercial symbol designating the franchisor or its affiliate; and
- (c) the franchisee is required to pay, directly or indirectly, a franchise fee."

Other jurisdictions in the United States have attempted to resolve the problem by more elaborate definitions, obviously designed to ensure that particular offenders will not escape the legislative net. As our report was in its final stages of preparation, a franchise act was introduced into and passed by the Legislative Assembly of Alberta, and in that Act, a definition similar to the California definition was adopted. In our view, the Massachusetts Act is too broad, encompassing as it may, many relationships which are not franchises in the accepted sense, and the California and Alberta definitions are better, except that we disapprove of clause (c) of the California definition (copied into the

Alberta Statute) rendering a fee an essential of the relationship. In our view, the fee is not essential, and to make it so would not only exclude many existing relationships where great control is exercised by the franchisor over the franchisee, but would also create a temptation to present franchisors to exempt themselves from the legislation by the simple expedient of eliminating that fee. Certainly some reward must accrue to the franchisor from the relationship. We cannot conceive of a situation where there will be no such reward, and it is not important whether that reward is in the form of a cash deposit at the time of obtaining the franchise, or is in some other form throughout the relationship.

We might just add that there are other aspects of the California and Alberta legislation (such as exemptions for companies holding large assets or having many franchisees) that did not appeal to us, and we are not recommending the adoption of that legislation. We are merely approving of the definition in part. In our view there is good reason not to exempt large corporations. Many of the complaints that came to our attention concerned these very companies, and the California and Alberta Acts, relying as they do mainly on full disclosure, serve only to regulate the smaller companies where the chief evils are deceptive selling practices and financial irresponsibility. A very major problem, however, in our view, is that involving contractual inequality, and in that respect the large corporations are by their very nature the chief offenders.

General Problems

(i) Contractual inequality and collective bargaining

We doubt very much if any legislation would be necessary, or, indeed, if any consideration to the legal problems of the relationship would ever have been given if the parties had been

able to bargain from positions of equal or relatively equal strength. The truth is that franchisors grant the franchises on contracts drawn for and in the interests of the franchisor and as a result, the inequities described below take place. This does not mean, of course, that there are not many happy franchisees, just as in feudal days there were many happy serfs, and there were many happy tenants prior to the enactment of Part IV of The Landlord and Tenant Act. But the inequality of bargaining power does produce inequitable contracts almost inevitably, and even where honest attempts have been made to redress the balance between the parties, there remain too many opportunities for repression that would not exist if the franchisee could freely contract his own bargain. It is probably impractical for a franchisor to grant concessions to one franchisee that he does not grant to all, and he cannot repose in all of them the same trust as he might in one or two. Most franchisors discourage collective bargaining, and the dealers' organizations which do exist are not effective to resolve this problem. We have considered some form of collective bargaining legislation, but we realize that it goes against the grain of the whole course of labour legislation in this province, which is limited to the rights of employees and has never been extended to the rights of more or less independent businessmen. We could, of course, recommend that no franchise contract should discourage collective bargaining, but we doubt if any such recommendation would be effective. The discouragement permeates the whole relationship and not just the contract, and we doubt if dealers' organizations could do the job required of them short of, at least,

some legislation in the nature of compulsory bargaining. It raises a whole host of problems and it is our hope that the recommendations we are making will better resolve the problem.

(ii) Termination and assignment

Throughout the evidence it was a recurring complaint that the franchisee is constantly plagued with the threat of termination of the franchise. Almost all franchise contracts give to the franchisor either an unfettered right to terminate or a right to terminate upon breach of the agreement, and it is all too easy for the franchisee to be in such breach. Whether there is a franchise fee or not, the franchisee has invariably invested time and money, and he knows that he will lose it all if the franchise comes to an end. Naturally, he is prepared to be servile, and if not, he is generally not long for the franchise family. We fully appreciate that the franchisor has much to lose in permitting the continued operation of the franchise, where the franchisee is adversely affecting the value of the trade mark or trade name. We know also that there are many instances of franchisees who should not be permitted to continue the operation of the franchise in any circumstances, and that speed in their removal may be essential. We also appreciate that it is of vital concern to the franchisor who succeeds to the operation of the franchise. At the same time, it is essential to the franchisee that he can reasonably transfer his interest and thus recoup his investment, and that his estate's rights on death or incompetency be protected. These conflicting interests we have attempted to resolve in our recommendations. In short, we have placed no limitation upon the rights of the

franchisor to terminate, but have given a remedy to the franchisee if such termination should be unjust.

(iii) Coercion and secret profits

Linked with the threat of termination is the forcing of franchisees into marketing schemes not of their own making. Often a franchisee is subjected to unreasonable and arbitrary sales and "share of market" goals or victimized by marketing strategy over which he has no control, which arises out of competition between his franchisor and others in the same market. While it would seem reasonable that a franchisor should be able to control the general franchise market for the welfare of all the franchises, nevertheless, the result sometimes is very detrimental to a particular franchisee, and he has no alternative but to follow the franchisor's instructions under the threat of termination.

Also, in many instances the profit of the franchisor largely runs from the sale to the franchisee of ingredients or raw material or supplies and equipment for the operation of the franchise. To the extent that these products are essential to that operation, there can be no complaint, but in many instances there seems to be no particular merit in the product required, and there also appear to be large profits in the form of secret rewards granted to the franchisor by the vendor of the product. The problem is one that is before the Courts in the Jirna v. Mister Donut case, and it may or may not be that franchisors will be required in law to disgorge any secret profits

so obtained. In the State of Indiana, the proposed law would resolve the problem in favour of a mutual fiduciary relationship described as follows:

"Between the franchisor and the franchisee there exist mutual fiduciary obligations, as though the parties had a relationship of mutual agency. This relationship requires, but is not confined to, the disclosures required by (this act) and any material changes disclosed under (this act)".

The Courts of this province and country may, of course, eventually resolve the problem in a manner akin to the proposed Indiana legislation, but it is our view in any event that there is an element of unfairness in requiring a franchisee to purchase from a particular source where there is no distinction in the product. We also believe that there may be an element of unfairness in the profits accruing to the franchisor from such forced sales. Our recommendations are designed to help resolve these problems.

(iv) Competition and discrimination

There was much complaint on the part of franchisees concerning the tendency of franchisors to operate competing businesses, directly or indirectly, or to discriminate between franchisees with regard to price, etc. In large part this is, of course, a federal jurisdictional problem and should be governed by The Combines Investigation Act or amendments thereto. It may, however, have some relevance to provincial legislation and to our recommendations, in that it might be unfair for a

franchisor to terminate a franchise on the basis of failure of the franchisee to achieve prescribed sales when his failure is due to the competitive or discriminatory practices of the franchisor. The problem is aggravated often by assurances given by the franchisor to the franchisee at the time of the making of the contract that there will be no competition to the franchisee in the distribution of the product. The assurance is not carried into the contract and is often not honoured in practice.

(v) Inducement and advertising

The element of high-pressure salesmanship is not so obvious here as in referrals and multi-level sales, but it exists nevertheless, and it is our view that control should be exercised over the advertising programmes and over the sales pitches of the franchisors. We have seen many questionable enterprises advertised in very respected publications. In our view, the matter can best be handled by the prospectus approach and by the advertising regulations we recommend.

(vi) Financial irresponsibility of franchisors

Again, this problem is not so common as in multi-level sales, but there have been instances of large franchise fees being paid in anticipation of services to be rendered by the franchisors in setting up the franchise business and of default on the part of the franchisors. Obviously this should be avoided if possible, and it can be avoided, in our view, by the same prospectus approach and an escrow of fees or bonding of franchisors. Indeed, this would appear to be the main object of much of the other legislation we have reviewed. While we concede that it

is a serious problem, we consider that it is only one of many problems to be solved.

Particular problems

(i) The Oil Industry

The oil industry is perhaps the most investigated of all franchise industries, and despite these investigations the complaints keep coming, and formed a large part of our hearings.

There have been at least eight reports of The Restrictive Trade Practices Commission under the authority of The Combines Investigation Act and at least four provincial enquiries involving British Columbia, Alberta, Nova Scotia and New Brunswick. The most comprehensive of these provincial reports was the Alberta Gasoline Marketing Report of December, 1968, under the Chairmanship of Kenneth A. Mackenzie, Q.C. This report recommended a form of Bill of Rights for gasoline dealers, including the following:

- (a) Security of tenure and freedom from arbitrary termination or increase in rent
- (b) The right to collective bargaining to determine hours of sale, etc.
- (c) The right to buy, and display or advertise, accessories of their choice
- (d) The right to prepay or pay out in full any debt owing to the company
- (e) the right to receive any tickets or prizes from the company which are part of a provincial or national sales campaign, free of charge
- (f) The right to buy and sell any gasoline he chooses.

The report also contained many prohibitions and restrictions upon the oil companies, mainly to ensure the rights of the dealers, but the Report was never acted upon, in part because the Provincial Government deemed it to be a Federal concern.

The brief and evidence of the Ontario Retail Gasoline and Automotive Service Association, in addition to supporting the adoption of the recommendations in the Alberta report, laid a great emphasis upon alleged competitive and discriminatory practices, and recommended the abolition of the sales gimmicks, e.g. "Power Players" of Esso, medallions of Shell, etc. as was proposed for enactment in Nova Scotia, but which Bill is now withdrawn. These competitive practices are justified by the oil companies upon the basis that customers require different types of service, some being dependent upon the security of brand name gasoline and service, and others being less dependent and more concerned with the economics of the service. In other words, some customers seek a brand name for its gasoline and service and are willing to pay more, and other customers are not so concerned, and want to pay less. Consequently, the oil companies have set up subsidiaries of their own which sell gas more cheaply, and also they sell to non-branded companies at prices lower than that at which they sell to their own licenced outlets. The difficulty with the whole argument is that the gasoline supplied appears to be the same or substantially the same in all of the outlets, and as this becomes known to the public, the dealers must inevitably suffer. O.R.G.A. takes the position that the whole problem could be largely solved by permitting dealers to market

competitive brands. This would obviously be anathema to the oil companies, it might well be suicidal to the dealers themselves, and is probably impractical. In any event, its effect on the consumer is not clear. We doubt if there would be much adverse effect so far as quality is concerned, because most gasolines and ancillary products are similar. The control, however, by one company of a chain of outlets, and the desire of that company to preserve its good name, may result in better service.

Some of the problems of this industry may be resolved by our recommendations, but we cannot pretend that they will solve all the problems. Many of them are problems that can be dealt with only by federal legislation and it may be that in addition to the general recommendations of this report, some special consideration should be given in Ontario to this particular industry. It is interesting that the Alberta legislation effectively excludes any regulation of the oil industry by exempting large corporate franchisors. We are firmly of the view that the oil industry should not be exempted from the legislation.

(ii) The Automotive Industry

It is interesting that the first nationally prominent franchise legislation in the United States was the Automobile Dealers Day in Court Act, which was designed to alleviate the plight of the automobile dealers only, and the Massachusetts legislation so far enacted, which is perhaps the most comprehensive franchise legislation in the world, is devoted solely to the interests of the automotive industry. In our hearings, the automobile dealers requested

legislation precisely similar to the Massachusetts Act and dealing with them alone, and the automobile manufacturers generally argued that their franchises are unlike ordinary franchises and required no legislation at all.

We cannot recommend that the Massachusetts legislation be incorporated as an Ontario statute, partly because there are constitutional difficulties, but more because, as will be seen, we do not believe in the single industry approach, and we do not believe that the motor car dealers require particular legislation. In the United States, the automobile dealers are perhaps more vocal than any other franchisee organization, and in addition to the Massachusetts Act, there are acts in more than a dozen states of the United States specifically dealing with the problems of this industry. The franchise relationship is well-developed in Ontario and yet the problems of the motor car dealers do not loom so large.

One problem, however, did concern us, and that was relating to the settlement of disputes. There seems to be no effective provision for the settlement of disputes between dealer and manufacturer in Canada. Some very involved procedures have been set up in the United States by the major companies, including in one case at least the provision of independent arbitrators. But similar arrangements have not been worked out here. It is stated by the manufacturers that this is because of a paucity of disputes, and that may be so, but the result is that high-level disputes must go to Detroit to be resolved. In our view this cannot be healthy for the development of the motor car industry

in this country, and certainly our recommendations will go some distance to eradicate the custom.

There are many problems indigenous to the automobile industry that will not be solved by our legislation, and some of these problems can be readily seen by examining the details of the Massachusetts legislation. We believe, however, that our proposals will assist in resolving some of the greater problems.

(iii) The Fast Food Industry

While we had remarkably little representation from franchisees of this industry either in the open or closed hearings, nevertheless, the questionnaires submitted indicated considerable disappointment, and many of the briefs received were in the same vein. It is undoubtedly the common public view that most of the commercial franchises are in this industry, but, in fact, we have found that many of the best-known fast food enterprises are, in fact, company owned, or in the hands of a single Ontario franchisee. Obviously for these no problems exist, and for the others we are content to suggest that the general provisions we are recommending will help to resolve their problems.

(iv) Small Investor Franchises

There are a great variety of small investor schemes involving in many cases the sale of equipment as part of a marketing plan. They are designed for the franchisee without experience, making a small investment in the hope of earning additional income in his spare time.

Examples of these are vending machines, pizza and sandwich enterprises and coat check concessions and janitorial services. The main difficulty with these schemes is that where merchandise is involved it is often over-priced, unproductive and of unmerchantable quality, and often the franchisors are financially irresponsible. The recommendations dealing with disclosure and advertising will assist to resolve the problems of these franchises.

(v) The Becker Problem

Much time in our hearings was devoted to hearing complaints by former managers of the Becker Milk Company of mistreatment or alleged mistreatment by the company. Some considerable time, also was spent in hearing from present satisfied Beckers managers. The Becker company itself did not give evidence, but submitted a brief to us in which, *inter alia*, it claimed that Beckers was not a franchisor and the problems of its managers should not be considered by our Committee.

So far as the Becker franchise argument is concerned, we are inclined to agree. The arrangement between the company and the managers is that the manager puts down a deposit (for good performance) and then is permitted to operate the store. He operates it as his own enterprise to the extent that he hires staff, makes the purchases and is responsible for any shortages, but it is nevertheless a Beckers store, and the profit or loss (other than inventory shortages) is the profit or loss of Beckers. There may be an argument that the relationship is one of franchise, and certainly Beckers at one time advertised on a basis akin to the disposition of

a franchise, but in our view the relationship is no more than an employment contract with a deposit for good behaviour and provisions for the forfeiture of that deposit in certain circumstances.

Regardless, however, of the nature of the relationship, the operation of the deposit and its forfeiture gives us some cause for alarm. The evidence was replete with stories of inventory checkers employed by Beckers descending upon the store at odd hours, taking inventory and finding shortages whereupon the company would forfeit the deposit, and also sometimes set off the salary owed to the manager against the alleged deficiency. We realize that an employer must have a right to terminate the engagement of a dishonest employee, but we seriously doubt that any of the instances before us had anything to do with dishonesty. The trouble was that there was no check on the adequacy of the accounting, and the manager's only remedy would be to take the matter to Court if he hoped to recover any part of his deposit and arrears of wages. In our view, deposits of this nature should not be subject to arbitrary and unilateral forfeiture. We believe that the deposit should be held in escrow to protect against the defaulting manager, but that the burden should be upon the store to show that there has been, in fact, default or loss suffered, and the manager should be entitled to at least the benefit of an independent auditor before suffering that forfeiture.

One suggestion to deal with the matter would be to amend The Employment Standards Act to place such deposits in a statutorily created trust,

permitting the employer to forfeit the deposits only upon the following conditions,

1. Service of a Notice of Intention of Forfeiture with reasons therefor upon the employee and also the Director under the Act.
2. The failure either of the Director or the employee to contest successfully the proposed forfeiture in the Courts (Provision will have to be made permitting such application either by the Director or the employee and prescribing time limits, etc.)
3. Wherever such forfeiture is by reason of an alleged shortage, the filing of an affidavit of accuracy or an auditor's certificate relating to such shortage.

We would suggest in any event that the employee's deposit should be recoverable in priority to any other creditor, and that any rights of the employee at law should be preserved. It may be also that such regulations should apply only to deposits of a substantial amount, say over \$50.

In short, we do not believe in the circumstances that the Becker problem comes within our terms of reference. Indeed, we doubt if it comes within the terms of reference of the Department to which we report. Nevertheless, we respectfully suggest that legislation be considered to deal with it.

Legislative approach

(i) Legislation or not?

Before even considering the type of legislation, we must determine whether any legislation is necessary. More than one witness beseeched us not to burden their lives further with regulations. They were conducting themselves and their businesses honourably, and for them and their companies, no legislation was necessary. Counsel for another franchisor emphasised that legislation is like cement, and that what may be desirable for some, and at least innocuous for the rest now, may be undesirable and burdensome in the future. We sympathize with and respect both views, but we believe that the evils cry out for some control. It shall be our purpose to recommend controls that are the least burdensome and the most flexible, while at the same time being consistent with the suppression of the evils of the system.

(ii) Generic or single-industry legislation

As reported earlier, the approach taken in Massachusetts, and under the U.S. Automobile Dealers Day in Court Act is a single industry approach, in each case dealing with the automobile industry. This is an approach often favoured by a particular industry, depending upon whether the particular industry seems more or less in need of regulation. Where the franchisees are more vocal, legislation for that industry is passed; where the franchisors have the stronger voice, that industry is by-passed. To us, this approach is wrong. It is inadequate if all industries are not covered, and it is

unnecessary to cover each industry separately. Admittedly there are differences in the present administration of franchises in different industries, and there are problems more pertinent to some. But these problems are transitory and, in our view, the basic problems are common to every industry involved in franchises. In any event, it is our desire to avoid specifics, as will be seen, and we therefore favour the generic approach.

(ii) Contractual v. equitable approach

Throughout this type of legislation we see two different threads, although sometimes the two threads are tangled and almost indistinguishable. One thread is the compulsory contract or contractual terms approach, whereby certain terms are made compulsory or rendered inoperative. Very simply put, this solution either prohibits certain contractual terms, e.g. arbitrary termination, or requires or reads in certain contractual terms, e.g. rights of renewal, assignment, etc. The defects of this approach are the enormous difficulties in covering all the abuses, the complexity of the legislation if it is to be effective (with the consequent frustration on the part of honest franchisors) and the anticipated ingenuity of the very franchisors we seek to control in devising contractual terms to subvert the intent of the legislation.

The other proposal is the "fair dealing" or "good faith" approach, which is exemplified vaguely in the U.S. Automobile Dealers Day in Court Act of 1956, and more specifically in the Massachusetts Auto Dealers Act of 1970. The

latter reinforces the "fair dealing" concept with very extensive examples of unfair practices, and this in effect combines both the fair dealing and contractual approaches. The main difficulty with the "fair dealing" approach is one of definition, with the result that any litigation based upon legislation of that sort is necessarily unpredictable, and litigants and counsel are naturally loath to undertake protracted and expensive litigation without some reasonable assurance of success.

We believe that a compromise solution is possible that will do much to solve the problem without creating new ones. It involves (in addition to administrative control discussed below):

1. Adopting generally the "fair dealing" approach.
2. Providing very limited terms and prohibitions in the dealings between the parties.
3. In these dealings also, placing the burden upon the franchisor to prove,
 - (a) that the contract is fair; and
 - (b) that the franchisor's exercise of his rights under the contract is justified in the circumstances.
4. Giving in the first instance to a quasi-judicial tribunal (subject to the constitutional problem discussed below) the right to determine the issues in 3, and with power to that tribunal to enlist expert assistance as required.

(iv) Administrative Control

Franchises run the gamut from the large international corporations to local individual entrepreneurs, and from those involving large investments, either in fees or capital expenditure or both, to those involving little expenditure of time or effort, but in all there is inevitably some expenditure of time or money by the franchisee, and we believe that such investment should be protected at least to the extent that the investor has the opportunity of knowing what he is investing in and the chances of a complete loss of investment is minimized. In short, we believe in full disclosure, and in control of the franchisee's investment. To that end, we are recommending a prospectus and an escrow arrangement with regard to franchise fees.

We further believe that a body is necessary to perform the various functions needed, which can be summarized as follows:

- (a) To receive and approve the prospectuses.
- (b) To protect, where necessary, the franchisee's investment
- (c) To educate investors or franchisees
- (d) To process complaints of inequities
- (e) To police the operation of franchisors.

(v) Recommendations

We therefore recommend:

1. The formation of a Franchise Bureau with a Franchise Registrar. As indicated in the multi-level considerations, it may be that it would be appropriate to have a Registrar for both multi-level and franchise matters and that there be a separate act dealing with multi-level sales and franchise sales and a Registrar appointed under that act. We should re-emphasize here the importance of the man chosen to fulfill the post. In the franchise field, he will be concerned not only with some very sophisticated contracts, but will also have to deal with some of the largest corporations in the land.

There should also be granted original and/or appellate jurisdiction to the Commercial Registration Appeals Tribunal to deal with disputes between franchisors and franchisees. We have not overlooked the constitutional problem that faces us by reason of section 96 of the British North America Act, and it may be that for that reason our proposal with respect to the Tribunal will be impractical. If it is, then, of course, resort must be had to the Courts. In our view, however, there is merit in using the Tribunal mainly because for franchise problems, a certain amount of expertise will be required, and the Tribunal is so devised that such expert assistance is readily at hand in the members thereof. There should always, of course, be an appeal either to the Divisional

Court or the Court of Appeal from the decisions of the Tribunal, but if this is not sufficient to satisfy section 96, the access to the Courts in the first instance will have to be made either alternative or complete.

It may be necessary, in order to implement these recommendations, in addition to the powers given to the Tribunal by paragraphs 8 to 10 below, to expand generally its field of operations as set forth in the Department of Financial and Commercial Affairs Act.

2. There should be a definition of "franchise" in accordance with the principles set out above. We also feel there should be a prohibition against the use of the word in commercial dealings not coming within the definition. The word "franchise" has a sort of independent businessman connotation and, when used indiscriminately in advertising or promotion, tends to deceive the investor to his detriment.
3. There shall be a prohibition of the dealing in franchises without compliance with the provisions below.
4. Every franchisor shall be required as a condition of dealing in franchises to file with the Registrar a prospectus, which prospectus shall include:
 - (a) The name of the franchisor, the name under which the franchisor is doing or intends to do business, the name of any parent or affiliated company that will engage in business transactions with franchisees.
 - (b) The franchisor's principal business address.

- (c) The business form of the franchisor whether corporate, partnership or otherwise.
- (d) The business experience of the franchisor, including the length of time the franchisor,
 - (i) has conducted a business of the type to be operated by the franchisee;
 - (ii) has granted franchises for such business;
 - (iii) has granted franchises in other lines of business.
- (e) The names of persons affiliated with the franchisor, including directors and officers, and such information concerning the identity and business experience of such persons, including past business records, as the Registrar may require or the Regulations prescribe.
- (f) A statement as to whether the franchisor or any person identified in the prospectus has been convicted of any criminal offence or has been held liable in any civil action by final judgment involving fraud, or is subject to any currently effective order or ruling of any provincial or dominion or United States state or federal commission or agency.
- (g) A recent financial statement of the franchisor, together with a statement of any material changes in the financial condition of the franchisor from the date thereof. The Regulations may prescribe,
 - (i) the form and content of financial statements required hereunder;
 - (ii) the circumstances under which consolidated financial statements shall be filed; and
 - (iii) the circumstances under which financial statements shall be audited.

- (h) A copy of the typical franchise contract or agreement proposed for use or in use in Ontario.
- (i) A statement of the franchise fee charged, if any, the proposed application of the proceeds of such fee by the franchisor and the formula by which the amount of the fee is determines if the fee is not the same in all cases.
- (j) A statement describing any payments or fees other than franchise fees, if any, that the franchisee is required to pay to the franchisor, including royalties, payments or fees which the franchisor collects in whole or in part on behalf of a third party or parties.
- (k) A statement of the conditions under which the franchise agreement may be terminated or renewal refused, or re-purchased at the option of the franchisor, together with a statement as to the rights of the parties upon the death, incapacity or insolvency of the franchisee, and whether the franchisee may voluntarily terminate, and upon what terms, and whether the franchisee is able to see the franchise, and if so, upon what terms.

(This may seem unnecessary, as the terms will be disclosed in the contract, but it is of such vital importance that we believe it wise to re-emphasize it)

- (l) A statement as to whether by the terms of the franchise agreement or by other device or practice, the franchisee is required to purchase from the franchisor or his designate, services, supplies, products, fixtures or other goods relating to the establishment or operation of the franchise business, together with a description thereof.
- (m) a statement as to whether the franchisor has either by contract, agreement, arrangement or otherwise, agreed with any third party or parties that the products or services of such third party or parties will be made available to the franchisee or franchisor on a discount or bonus basis, and details thereof.

- (n) A statement as to whether by the terms of the franchise agreement or other device or practice, the franchisee is limited in the goods or services which may be offered by him to his customers, and details thereof.
- (o) A statement of the terms and conditions of any financing arrangements relating to the sale of the franchise, when offered directly or indirectly by the franchisor or his agent or affiliate.
- (p) A statement of any past or present practice of or any intent of the franchisor to sell, assign or discount to a third party any note, contract or other obligation of the franchisee in whole or in part.
- (q) A statement of the number of franchises at present operating and proposed to be sold within the next year after registration.
- (r) A statement as to whether the franchisees receive any exclusive rights of territory, and if so, the extent thereof.
- (s) A statement of any compensation or other benefit given or promised to a public figure, arising in whole or in part from,
 - (i) the use of the public figure in the name or symbol of the franchise; or
 - (ii) the endorsement or recommendation of the franchise by the public figure in advertisements.
- (t) A statement as to whether any procedure has been adopted by the franchisor for the settlement of disputes between the franchisor and the franchisee, together with details.
- (u) A statement as to whether the franchisor provides continuing assistance in any form to the franchisee and if so, the nature, extent and cost thereof.
- (v) A statement of the training responsibilities of the franchisor.

- (w) A statement of any competitive activities that have been, are or may be entered into by the franchisor, its agents or affiliates, directly or indirectly, together with details.
- (x) A statement of any restrictive covenants on present or future business activities of the franchisee.
- (y) A statement of the names and addresses of former franchisees in the province who have assigned, sold, transferred or voluntarily terminated, or have been terminated within the year preceding registration.
- (z) Such other information relating to the application as the Registrar may reasonably require or as the franchisor may desire to present.

In listing the information required for the prospectus, we have borrowed heavily from the California and Alberta legislation. We have, however, amended many, deleted some and added a few of our own. The list is now, in our view, comprehensive enough to disclose every evil that we have discovered in the course of our investigation. It is to be noted that the California and Alberta statutes really go no farther than full disclosure. We believe that further safeguards and remedies should be given, and we offer them in the following paragraphs.

5. The Registrar may accept or refuse to accept the prospectus (subject to appeal to the Tribunal) and if he finds that the applicant has failed to demonstrate that adequate financial arrangements have been made to fulfill the obligations set forth in the prospectus, may order an escrow of fees charged to the franchisee, or the posting of bonds by the franchisor to cover possible loss.

6. There shall be filed with the Registrar all variations in the prospectus, and annually an audited financial statement and an affidavit with respect to changes, similar to the provisions affecting multi-level schemes - see paragraphs numbered 5 and 6 on pages 31, 32, *infra*.
7. The Registrar shall have the right to cancel the registration and the right of the franchisor to deal in franchises, similar to section 6 of the amended Consumer Protection Act, and there might be provision for injunctions as suggested in paragraph 10 of the recommendations relating to multi-level sales.
8. Before trading in any franchise, the franchisor shall provide the prospective franchisee, at least 48 hours prior to the execution of the franchise agreement, with a copy of the prospectus, together with a copy of all proposed agreements relating to the sale of the franchise. If such documents are not provided as required, the franchisee may rescind the contract at any time up to the receipt of the documents and 48 hours thereafter.
9. In all dealings between franchisors and franchisees, whether before, during or upon the termination of the franchise, the franchisor shall deal fairly with the franchisee, and it shall be open to the franchisee at any time to apply to the Tribunal (or to the Court or to either - see paragraph 1 under Recommendations, *supra*) for a determination of the rights

between the parties, and upon such hearing, the burden shall be upon the franchisor to show:

- (i) the contract between the parties was fair; and
- (ii) the franchisor's conduct was equitable in the circumstances.

10. The Tribunal shall have all powers, both legal and equitable, to excuse the franchisee from performance of any contractual term, with or without the imposition of terms upon the franchisee, and to enjoin the franchisor from the exercise of any of his rights under the contract, and may make interim or ex parte orders pending the hearing.

11. (1.) In determining whether or not the terms of the contract are fair or the conduct of the franchisor is equitable in the circumstances, the tribunal shall have regard in normal circumstances to the elimination of the following practices:

- (a) arbitrary termination of the franchise;
- (b) arbitrary refusal of assignments or renewals of the franchise;
- (c) arbitrary refusal of permission to dispose of franchises upon death or incapacity of the franchisee;
- (d) the obligation to purchase raw materials or other materials necessary to the operation of the franchise from a particular source;
- (e) arbitrary forfeiture of deposits or fees;

- (f) competitive practices of the franchisor detrimental to the welfare of the franchisee;
- (g) discouragement of collective bargaining practices among franchisees.

(2.) The Tribunal shall have power to prohibit any conduct of the franchisor if such conduct is contrary to assurances given at the time of entering into the contract, whether or not such assurances are carried into the contract or contradicted thereby.

12. No franchisor shall publish any advertisement offering a franchise unless a true copy of that advertisement has been filed with the Registrar at least three days prior to publication thereof. Where the Registrar is of the opinion that any advertisement contains false, misleading or deceptive statements, he may order that it be not published or that it immediately cease to be published.

13. No franchisor shall make any statement, representation or prediction with respect to earnings or projected earnings, either by advertising or otherwise, unless he at the same time and in the same manner sets forth the basis of and the method of calculation of such earnings or projected earnings.

14. Wherever by contract the franchisor exacts funds from the franchisee for advertising purposes, he shall be required to make a true accounting of the expenditure of such funds within a reasonable time after their levy.

15. Any condition, stipulation or condition purporting to bind any person acquiring any franchise to waive compliance with any provision of this Act or any regulation thereunder, is void.

SUMMARY OF RECOMMENDATIONS

The following is a brief resume of the major recommendations of this report, without precision or detail.

| | <u>Item</u> | <u>Page</u> |
|--|---------------|-------------|
| <u>Referral Sales</u> | | |
| 1. Extension of liability to original Ontario distributor and/or selling company | 3 | 14 |
| 2. Form of contract to be approved | 4 | 14 |
| 3. Contract to be entitled "Referral Sales or Lease Contract" and to contain referral element as a promise of seller | 6(a) & (b) | 15 |
| 4. Right of purchaser to rescind within seven days | 7 | 16 |
| 5. Registrar may cancel licenses where seller deceives purchaser or fails to carry out services or warranties | 8 | 16 |
| 6. Seller's rights for non-payment limited to seizure of goods | 9 | 17 |
| 7. Prohibition of cut-off clause | 10 | 18 |
| <u>Multi-level or pyramid sales</u> | | |
| 1. No scheme to operate except as provided | 3 | 29 |
| 2. Promoter to file prospectus setting out information on scheme before commencing to sell | 3 | 29 |
| 3. Report subsequent changes | 5 | 31 |

| | | | |
|----|---|----|----|
| 4. | Promoter cannot operate unless, | | |
| | (a) product immediately available; | | |
| | (b) investor gets product to retail value of his investment; | | |
| | (c) finder's fees limited to 10% | 4 | 30 |
| 5. | Investor to have compulsory 48-hour cooling-off period after receipt of contract and before signing | 7 | 32 |
| 6. | Investor can rescind within six months and get 75% of investment returned | 8 | 32 |
| 7. | Promoters to maintain register of investors | 10 | 33 |

Franchises

| | | | |
|----|--|------|----|
| 1. | Legislation to apply to all industries and to all franchises within each industry | (ii) | 52 |
| 2. | Prohibition against dealing in franchises except as provided | 3 | 57 |
| 3. | Franchisor to file prospectus setting forth detailed information on scheme | 4 | 57 |
| 4. | Franchisee to have compulsory 48-hour cooling-off period before execution of agreement | 8 | 62 |
| 5. | Franchisee to have right to apply to Tribunal or Court to determine, | | |
| | (a) whether contract is fair; and | | |
| | (b) whether conduct of franchisor is fair in circumstances | 9 | 62 |
| 6. | Tribunal or Court to discourage following: | | |
| | (a) arbitrary termination | | |
| | (b) arbitrary refusal of assignments or renewals | | |
| | (c) arbitrary forfeiture of deposits | | |

| | <u>Item</u> | <u>Page</u> |
|---|-------------|-------------|
| (d) forced purchases and secret profits | | |
| (e) competitive and discriminating practices by franchisors | 11 | 63 |

General

| | | |
|--|----|----|
| 1. The formation of a separate branch of division with its own Registrar to administer multi-level and franchise matters | 1 | 26 |
| | 1 | 56 |
| 2. Control of advertising | 3 | 29 |
| | 13 | 34 |
| | 12 | 64 |
| 3. Regular renewal of permission to operate to be required | 6 | 31 |
| | 6 | 62 |
| 4. Suspension and cancellation of permission to operate | 11 | 34 |
| | 7 | 62 |
| 5. Regular inspection of records | 5 | 31 |
| | 12 | 34 |
| | 6 | 62 |
| 6. Provision for escrow of investments or fees to protect investors and franchisees | 9 | 33 |
| | 5 | 61 |
| 7. Application of legislation to leases as well as sales | 2 | 13 |

APPENDICES

| | | Page |
|-------------|--|------|
| Appendix 1 | Statement to the Ontario Legislature by the Minister of Financial and Commercial Affairs re Minister's Committee on Franchising | 70 |
| Appendix 2 | Notice of Hearings | 71 |
| Appendix 3 | Dates and Location of Hearings and List of Witnesses appearing at Public Hearings on Referral and Multi-Level Selling Practices | 72 |
| Appendix 4 | Dates and Location of Hearings and List of Witnesses appearing at Public Hearings on Franchising | 74 |
| Appendix 5 | Dates and Location of Private Hearings on Referral and Multi-Level Selling Practices and Franchising | 76 |
| Appendix 6 | Briefs submitted on Referral and Multi- Level Selling Practices | 77 |
| Appendix 7 | Briefs submitted on Franchising | 78 |
| Appendix 8 | Bibliography | 79 |
| Appendix 9 | Franchisor Questionnaire | 82 |
| Appendix 10 | Franchisee Questionnaire | 90 |

APPENDIX 1

STATEMENT TO THE ONTARIO LEGISLATURE BY
THE HONOURABLE BERT LAWRENCE, M.C., Q.C.
MINISTER OF FINANCIAL AND COMMERCIAL AFFAIRS
JUNE 17, 1970, 2:00 p.m.

SUBJECT: MINISTER'S COMMITTEE ON FRANCHISING

I AM PLEASED TO ANNOUNCE THE ESTABLISHMENT OF A MINISTER'S COMMITTEE ON FRANCHISES WITH THE FOLLOWING TERMS OF REFERENCE:

"TO REVIEW AND REPORT UPON WHAT ARE COMMONLY DESCRIBED AS REFERRAL, PYRAMIDING OR MULTIPLE LEVEL SALES PRACTICES, ARRANGEMENTS AND FRANCHISES, AND TO CONSIDER ALL ASPECTS OF THE RELATIONSHIP OF FRANCHISORS AND FRANCHISEES AND THE IMPLICATIONS OF THESE ARRANGEMENTS TO THE CONSUMER AND THE INVESTOR AND GENERALLY TO RECOMMEND WHAT, IF ANY, CHANGES IN THE LAW ARE DESIRABLE".

THE MEMBERSHIP OF THE COMMITTEE WILL CONSIST OF A CHAIRMAN AND TWO MEMBERS CHOSEN FROM THE BUSINESS AND CONSUMER COMMUNITY. PROFESSOR WILLIAM A.W. NEILSON, OSGOODE HALL LAW SCHOOL, YORK UNIVERSITY WILL BE RESEARCH DIRECTOR AND COUNSEL TO THE COMMITTEE. MRS. D.A. STAFL, RESEARCH ECONOMIST OF THE DEPARTMENT OF FINANCIAL AND COMMERCIAL AFFAIRS WILL ACT AS SECRETARY TO THE COMMITTEE.

THE RESEARCH STAFF WILL COMMENCE WORK IMMEDIATELY COLLECTING AND ANALYSING MATERIAL TO BE PRESENTED TO THE COMMITTEE LATER THIS SUMMER. I INTEND THAT THE COMMITTEE WILL HOLD PUBLIC HEARINGS, RECEIVE BRIEFS AND REPRESENTATIONS AND REPORT TO ME ITS SPECIFIC FINDINGS AND RECOMMENDATIONS, AND I EXPECT TO RECEIVE THESE BEFORE THE YEAR'S END.

THE GLOBE & MAIL
Dec. 9/70

THE TORONTO STAR
Oct. 1/70

PUBLIC HEARINGS

MINISTER'S COMMITTEE ON FRANCHISES



A PUBLIC HEARING

ON REFERRAL SALES AND PYRAMIDING OR MULTI-LEVEL PRACTICES IN ONTARIO

Honourable Bert Lawrence, Q.C., Minister of Financial and Commercial Affairs of Ontario, has appointed a Committee to enquire into and report and make recommendations regarding the above practices, and any related matter.

REFERRAL SALES

Referral selling is a practice whereby certain door-to-door salesmen and others lead a consumer to believe that the purchase price will be defrayed in part, or that some reward will be given, by suggesting names of others who will also buy, test or use the product or service.

Certain problems suggested are:

- (1) Some of the articles or services appear to be sold at inflated prices.
- (2) In some instances the customer has not been made aware of the need to pay the full price regardless of his success in referrals.
- (3) Some customers do not appear to have been made to realize the mathematical improbabilities of unrestricted referrals.

PYRAMIDING OR MULTI-LEVEL DISTRIBUTING

Pyramiding or multi-level distributing is an arrangement whereby the original distributor recruits members of the public as investors to act as wholesalers or distributors, with a further right to those investors to recruit further investors-distributors for such purpose. This leads to a number of field representatives whose status within the organization is generally determined by the amount of money invested or inventory purchased.

Certain problems suggested are:

- (1) Some investor-distributors are not made aware that they become purchasers, not just salesmen, of the products.
- (2) Some investor-distributors are not made aware that there are no defined areas of operation for them, and the market may be saturated.
- (3) Some investor-distributors are not made aware of the mathematical limits to the sale of distributorships.

The Committee will be pleased to receive from any person or organization:

- (a) Briefs
- (b) Letters
- (c) Oral representations

Briefs and correspondence should be addressed to:

Mrs. D. A. Stafl,
Department of Financial and Commercial Affairs,
555 Yonge Street
Toronto 5, Ontario.

and should be delivered or mailed by October 15th, 1970. Any person or organization wishing to make oral representation should contact Mrs. Stafl for the purpose of arranging time, etc.

A PUBLIC HEARING WILL BE HELD on Monday, October 26th, and Tuesday, October 27th, 1970 at 10:00 a.m., 2:00 p.m. and 8:00 p.m., in the Huron Room, 2nd Floor, Macdonald Building, Parliament Buildings, main entrance Wellesley Street (between Bay Street and Queen's Park Crescent), Toronto.

Other hearings elsewhere in Ontario may be scheduled. Further information may be obtained from:

Mrs. D. A. Stafl—385-5151.

S. G. M. Grange, Q.C.)
Mrs. J. R. A. Turner) Committee
Watson W. Evans)
William A. W. Neilson)
Research Director and Counsel
Mrs. D. A. Stafl Secretary.

The Committee on Franchises will conduct a series of Public Hearings in January to provide an opportunity to individuals and organizations to present their views and experiences on franchising.

Franchising is a system whereby one person, a franchisor, authorizes another person, a franchisee, to distribute goods or services under a marketing plan devised by the franchisor. Under the franchise plan the franchisee uses the franchisor's trademark or other commercial symbol and maintains uniform practices outlined in the franchise agreement. Such plans are now common in many and varied types of businesses.

The Committee will consider all aspects of the relationship between franchisors and franchisees. Some problems suggested to the Committee concern the promotion, content, and method of termination of the franchise agreement.

Public Hearings will be held:

Monday, January 18, 1971—10:00 a.m. and 2:00 p.m.

Tuesday, January 19, 1971—10:00 a.m. and 2:00 p.m.

Wednesday, January 20, 1971—8:00 p.m.

Place: Huron Room, Second Floor, Macdonald Building, Wellesley Street, Toronto. Entrance: south side of Wellesley Street between Bay Street and Queen's Park Crescent.

The Committee will accept briefs, letters or oral presentations from individuals and organizations. Any person or organization wishing to make representation or requiring further information should contact in writing, or by telephone

Mrs. D. A. Stafl, Secretary to the Committee,
Dept. of Financial and Commercial Affairs,
555 Yonge Street,
Toronto 5, Ontario.
(416) 365-5151.

Written submissions should be filed in five copies, preferably not later than December 31, 1970.

Additional hearings may be scheduled if response warrants.

S. G. M. Grange, Q.C.—Chairman

Watson W. Evans

Mrs. J. R. A. Turner

Minister's Committee
Dept. of Financial & Commercial Affairs

APPENDIX 3

APPEARANCES AT PUBLIC HEARINGS ON REFERRAL AND MULTI-LEVEL SELLING PRACTICES

Evidence was received from the following persons, listed in the order of their appearances, on their own behalf or on behalf of organizations they represented. An asterisk beside a name indicates that a brief or submission was presented.

Hearings were held in the Huron Room, Macdonald Block, Wellesley Street.

October 26th, 1970 Mrs. S. Roman, purchaser of a Filter-Queen vacuum cleaner.

*Mr. S. Brody, General Manager, J. Marvin Limited, Compact and Vanguard Distributor.

*Professor Stephen Waddams, Faculty of Law, University of Toronto.

*Mr. T.G. Rimmer, Vice-President, Better Business Bureau of Metropolitan Toronto Inc.

*Mr. G.R. Manson, President, Swipe Products Ltd.

Mr. and Mrs. T. Toth, purchaser of a Filter-Queen vacuum cleaner.

Mr. Michael Sokulski, investor in Savex Cashchek Ltd.

Mr. K. Hopper, General Manager for Ontario, Savex Cashchek Ltd.

Mr. Michael Drainie, investor in Koscot Interplanetary of Canada Ltd.

Mr. and Mrs. John Lelis, purchaser of Filter-Queen vacuum cleaner.

Mr. Joe Gmainer, purchaser of Filter-Queen vacuum cleaner.

Mr. Mah Ming, law student, who appeared with Mr. and Mrs. J. Lelis and Mr. J. Gmainer.

Mr. Louis Szepflecki, student from Humber College of Applied Arts and Technology.

Mr. John Alexander, General Distributor, Holiday Magic, Inc.

Mr. Terry Connellan, General Distributor, Holiday Magic Inc.

October 27th, 1970 Mr. Donald Baker, law clerk with Gerald E. Vickers, Barrister, Solicitor & Notary Public.

*Mr. Vincent Forbes, General Manager, Better Business Bureau of the Mainland of B.C. and Vice-President of the Association of Canadian Better Business Bureaus.

Mr. Donald Wry, purchaser of an auto stabilizer through Pay-Lo Enterprises.

APPENDIX 3 CONT'D

***Mr. David L. Gibson, President, Direct Sellers Association.**

Mr. David Ongley, Chairman of the Legislative Committee, Direct Sellers Association.

Mr. David Ongley, Sales Manager, Filter-Queen Corp.Ltd.

***Mrs. H.R. Fisher, President, Consumers' Association of Canada, Ontario Division.**

Mrs. C.G. Barrick, Executive Member, Consumers' Association of Canada, Ontario Division.

Mr. S. Brody, General Manager, J. Marvin Limited, Compact and Vanguard Distributor.

Mr. Robert Hollow, President, Color Mutual of Canada.

Mrs. W.T. Weller, President, World of Color Television Ltd.

Mr. W.T. Weller, Treasurer, World of Color Television Ltd.

Mr. Warren Green, Director, World of Color Television Ltd.

Mr. Carlton Clarke, purchaser of a Comet vacuum cleaner.

APPENDIX 4

APPEARANCES AT PUBLIC HEARINGS ON FRANCHISING

Evidence was received from the following persons, listed in the order of their appearances, on their own behalf or on behalf of organizations they represented. An asterisk beside a name indicates that a brief or submission was presented.

Hearings were held in the Ontario Room, Macdonald Block, Wellesley Street.

January 18th, 1971 *Mr. W.J. Coke, Vice President and General Manager, Manpower Services (Ontario) Ltd.

Mr. J. McConnell, Assistant General Manager, Manpower Services (Ontario) Ltd.

*Mr. C.G. Kappler, Retail Sales Manager, Shell Canada Limited.

Mr. R.S. Aberg, Region Manager, Central Marketing Region, Shell Canada Limited.

*Mr. Albert St. Pierre, franchisee of Universal Travel Club.

*Mrs. C.J. Askew, Legislation Chairman, Consumers' Association of Canada, Ontario Division.

Mrs. N.A. Carrier, Executive Secretary, Consumers' Association of Canada, Ontario Division.

*Mr. Ken Langdon, Executive Secretary, The Ontario Retail Gasoline & Automotive Service Association.

Mr. Alick Ryder, solicitor for The Ontario Retail Gasoline & Automotive Service Association.

Mr. John Neville, operator of a Sunoco station in Windsor, The Ontario Retail Gasoline & Automotive Service Association.

January 19th, 1971 Mr. Victor Heyn, Mrs. F. McManaman, Mr. J. Fletcher, Mrs. Patricia Kitchen, Mr. Peter Schembri, Mrs. M. Szabo, Mrs. Audrey Gladman, Mr. W.F. Rand, Mr. H. Meyers, (former managers of The Becker Milk Co. Limited stores).

Mr. Meyer, Mr. Lockhart, Mr. Gamble, Mr. Forbes, (managers of The Becker Milk Co. Limited stores).

Mr. Victor Joanovits, franchisee of International Janitorial Services.

*Mr. Harold Brown, attorney-at-law, Boston, Massachusetts.

*Mr. H.W. Shea, Regional Sales Manager, Imperial Oil Limited.

Mr. W. Estey, Q.C., Counsel, Imperial Oil Limited.

Mr. Benjamin Dossik, distributor for Mr. Ivan Ltd.

APPENDIX 4 CONT'D

January 20th, 1971 Mr. Fred M. Catzman, Q.C., Solicitor.

*Mr. Robert P. Parker, Counsel for The International Franchise Association.

Mr. W.E. Potts, distributor for Sunway Distributing Ltd.

Mr. Donald Marsh, distributor for Sunway Distributing Ltd.

Mr. C. Jamieson, Deputy Registrar, Consumer Protection Bureau, witness, Sunway Distributing Ltd.

Mr. G. Putsey, landlord, Stop 29 Restaurants.

Mr. and Mrs. A. Bergart, former store manager for The Becker Milk Co. Limited.

Mr. A. Sajna, distributor for Sunway Distributing Ltd.

March 29th, 1971 Mr. Cliff Tompkinson, former franchisee of Volkswagen Canada Ltd.

APPENDIX 5

PRIVATE HEARINGS ON REFERRAL AND MULTI-LEVEL SELLING PRACTICES
IN ONTARIO WERE HELD AT THE DEPARTMENT OF FINANCIAL AND
COMMERCIAL AFFAIRS, 555 YONGE STREET,

October 22nd, 1970

PRIVATE HEARINGS ON FRANCHISING WERE HELD AT THE DEPARTMENT OF
FINANCIAL AND COMMERCIAL AFFAIRS, 555 YONGE STREET,

March 15th, 1971

March 29th, 1971

April 16th, 1971

April 19th, 1971

APPENDIX 6

LIST OF BRIEFS ON REFERRAL AND MULTI-LEVEL SELLING PRACTICES
SUBMITTED TO THE COMMITTEE

Association of Canadian Better Business Bureaus

Better Business Bureau of Metropolitan Toronto Inc.

Buycard Limited

Consumers' Association of Canada, Ontario Division

Consumers' Association of Canada, Kitchener Branch

Direct Sellers Association

J. Marvin Limited, Compact and Vanguard Distributor

Mr. John Saunders

Swipe Products Ltd.

Professor Stephen Waddams, Faculty of Law,
University of Toronto

APPENDIX 7

LIST OF BRIEFS ON FRANCHISING SUBMITTED TO THE COMMITTEE

Agro, Cooper, Zaffiro, Parente, Orzel & Hubar, Barristers and
Solicitors

Askew, Dorothy, Chairman, Legislative Committee, Ontario Division,
Consumers' Association of Canada

The Becker Milk Co. Limited - Statement

Brown, Harold, attorney at law, Boston, Massachusetts - Statement

Canadian Automatic Merchandising Association

Catzman, Fred M., Q.C., Barrister - Statement

Consumers' Association of Canada, Ontario Division

Dennis, Ernest, concerning Sunway Distributing Ltd.

Imperial Oil Limited

Johnston & Mandryk, Barristers & Solicitors

Manpower Services (Ontario) Ltd.

McKelvie, F.A., concerning United Scholarship Fund

Nabb, F.A. and Duffy, J.R., concerning Schertle International Limited

The Ontario Retail Gasoline & Automotive Service Association

Parker, Robert P., attorney at law, Brownstein, Zeidman, Drew &
Schomer, Washington, D.C., Statement on behalf of The International
Franchise Association

Fronto Petroleum Agents Incorporated

Raceco Automotive Limited

Red Barn System (Canada) Limited

Rubin & Jeffery, Barristers and Solicitors

Shell Canada Limited

Tilden Rent-a-Car System Ltd.

APPENDIX 8

BIBLIOGRAPHY

Books

"The Franchise Boom", by Harry Kursh, Prentice-Hall Inc., Englewood Cliffs, New Jersey, 1968.

"Franchise Company Data for Equal Opportunity in Business", U.S. Department of Commerce, Washington, D.C., 1969.

"A Franchise Directory", 1970 Edition, International Franchise Opportunities, 421 Center St., Lewiston, New York 14092 and 11 Bond Street, St. Catharines, Ontario.

"The Franchise Handbook 1970", by Jan Cameron, Crown Publishers Inc., New York, 1970.

"Franchising: A Trap for the Trusting", by Harold Brown, Little, Brown & Co., Boston, Mass., Revised 1970.

"Franchising: How to Select a Business of your Own", by Robert Metz, Hawthorn Books, Inc., New York, 1969.

"Franchising: The Odds-on Favourite", by J.F. Atkinson, BS, MBA, International Franchise Association, Chicago, Illinois, 1968.

"Franchising Today", Report of the Fifth International Management Conference on Franchising Sponsored by Boston College, Edited by Charles L. Vaughan, Ph.D., Farnsworth Publishing Company Inc., Lynbrook, New York, 1970.

"Gasoline Marketing in the Context of the Oil Industry", Report from The Gasoline Marketing Enquiry Committee to the Government of Alberta, 1968.

"Gasoline Marketing in Alberta", A reply to the Report of The Gasoline Marketing Enquiry Committee, by Imperial Oil Limited, 1969.

"Law and the Balance of Power", The Automobile Manufacturers and their Dealers, by Stewart Macaulay, Russell Sage Foundation of New York, N.Y. 10017, 1966.

"Partners for Profit, A Study of Franchising", American Management Association, Inc., New York, 1966.

"Profits from Franchising", by Robert M. Rosenberg with Madelon Bedell, McGraw-Hill Book Co., New York, 1969.

"The Realities of Franchising", by Harold Brown, Faneuil Press, Boston, Mass., 1970.

"Statement on Gasoline Marketing in the Context of the Oil Industry", by Shell Company Limited, 1970.

"Trends in Canadian Marketing", by M.S. Moyer and G. Snyder, Dominion Bureau of Statistics, Queen's Printer, Ottawa, Canada, 1967.

Periodicals

"Continental Franchise Review", Continental Reports Inc., P.O. Box 6360, Denver, Colorado 80206.

"Franchise Journal", Franchise Journal Corp., 892 W. 16th Street, Newport Beach, California 92660.

"Franchising Around the World", Sutton Place Publications, Inc., 159-15 Northern Blvd., Flushing, New York 11358.

"NAFB Letter - The monthly report on Franchising", National Association of Franchised Businessmen, 1404 New York Avenue, N.W., Washington, D.C. 20005.

"National Franchise Reports", 892 W. 16th Street, Newport Beach, California 92660.

Hearings

"The Impact of Franchising on Small Business", Report of the Select Committee on Small Business, United States Senate, based on Hearings before the Subcommittee on Urban and Rural Economic Development, January 20, 21, 22, 27, March 30, and April 24, 1970, U.S. Government Printing Office, Washington: 1970.

"The Impact of Franchising on Small Business", Hearings before the Subcommittee on Urban and Rural Economic Development of the Select Committee on Small Business, United States Senate, Ninety-first Congress, Second Session, Part 1, January 20, 21, 22 and 27, 1970, U.S. Government Printing Office, Washington: 1970.

"Franchise Legislation", Hearings before the Subcommittee on Antitrust and Monopoly of the Committee on The Judiciary, United States Senate, Ninetieth Congress, First Session, pursuant to S. Res. 26 on S. 2507 A Bill Relating to Dealings Between Parties to Franchise Agreements, S. 2321 A Bill to Supplement the Antitrust Laws of the United States in order to prevent anticompetitive practices, by providing for just compensation upon termination of certain franchise relationships, October 10, 11, 13, 16, 17 and 31 and November 1, 1967. U.S. Government Printing Office, Washington: 1968.

"Distribution Problems Affecting Small Business", Hearings before the Subcommittee on Antitrust and Monopoly of the Committee on The Judiciary, United States Senate, Eighty-ninth Congress, First Session, pursuant to S. Res. 40, Part 1, Franchising Agreements, March 2, 3, and 4, 1965, U.S. Government Printing Office, Washington: 1965; pursuant to S. Res. 191, Part 2, January 18, 19, 20, 26, and 27, 1966, U.S. Government Printing Office, Washington: 1966; pursuant to S. Res. 191, Part 3, on S. 2549, To amend the Sherman Antitrust Act to provide that exclusive territorial franchises, under limited circumstances, shall not be deemed a restraint of trade or commerce or a monopoly or attempt to monopolize, and for other purposes, June 21, 22, 23, and 27, 1966, U.S. Government Printing Office, Washington: 1967.

"Interim Hearing on Franchises", State of California, Senate Committee on Insurance and Financial Institutions, Sacramento, California, November 7, 1969.

Pamphlets

"Factors to Consider in Connection with Franchise Offers", Better Business Bureau of Metropolitan Toronto Inc.

"Facts about Franchising", National Better Business Bureau, 230 Park Ave., New York, N.Y. 10017, 1965.

"Franchising", Small Business Reporter, Bank of America, San Francisco, California, 1970.

"Much Ado about Franchisers", by Clark Pace, The Exchange, February 1970, The New York Stock Exchange.

Articles

Barron's

Four part series of articles on fast food franchising by J. Richard Elliott, Jr., August 25 - September 29, 1969.

Two part series of articles on fast food franchising by J. Richard Elliott, Jr., April 12 and 26, 1971.

Fortune

"Franchising's Troubled Dream World", by Charles G. Burck, March 1970, p. 116.

World

Peat, Marwick, Mitchell & Co., Summer 1970

"The Accountants' Stand on Franchise Reporting", by Thomas L. Holton and Olden J. Hoover.

The Journal of Accountancy, January 1970

"Accounting for Initial Franchise Fee Revenue", by Archibald E. MacKay.

Christian Science Monitor

Series of articles on "Franchising", May 18 - June 11, 1970 issues.

Business Lawyer

"Franchising - Changing Legal Skirmish Lines or Armageddon?", by Norman D. Axelrad, January 1971, p. 695.

Management Aids for Small Manufacturers, published by Small Business Administration, U.S. Government Agency.

"The Franchise System of Distribution", by E.H. Lewis, 1966

"Expanding Sales Through Franchising", by Al Lapin, Jr., 1968

"Are You Ready For Franchising", by A.L. Tunick, 1970

APPENDIX 9

THE DEPARTMENT OF FINANCIAL AND COMMERCIAL AFFAIRS

MINISTER'S COMMITTEE ON FRANCHISES

FRANCHISOR QUESTIONNAIRE

PLEASE COMPLETE AND RETURN BY JANUARY 31, 1971 TO:

Mrs. D.A. Stafl, Secretary
Minister's Committee on Franchises
Department of Financial & Commercial Affairs
555 Yonge Street
Toronto 284, Ontario

1. Name of Company _____
2. Address _____
3. Telephone Number _____
4. Officer of Company to contact re This Questionnaire _____
5. How is your Company organized? Check one:

| | |
|---------------------|-------|
| Sole Proprietorship | _____ |
| Partnership | _____ |
| Private Company | _____ |
| Public Company | _____ |
6. Provincially or federally incorporated? _____
If provincial, which province? _____
7. If there is a parent or controlling corporation, please state name and address:

8. Please check the category which most appropriately describes your franchise system. (*Please use separate questionnaire for each franchise program - extra copies available from address noted at outset).

| | |
|---|-------|
| Automobile Dealers | _____ |
| Automotive Parts/Services | _____ |
| Auto/Trailer Rentals | _____ |
| Beauty Salons | _____ |
| Boats, Snow and Terrain Vehicles | _____ |
| Business Services/Equipment | _____ |
| Children's Stores | _____ |
| Clothing/Shoes | _____ |
| Construction/Remodeling - Materials/Services | _____ |
| Cosmetics/Toiletries | _____ |
| Drug Stores | _____ |
| Educational Products/Services | _____ |
| Employment and Personnel Services | _____ |
| Entertainment/Recreational Centres | _____ |

8. Cont'd.

| | |
|------------------------------------|-------|
| Equipment Rentals | _____ |
| Food - Donuts, Pancakes, Waffles | _____ |
| Food - Ice Cream/Candy/Popcorn/ | _____ |
| Beverages | _____ |
| Food - Restaurant/Drive-Ins/ | _____ |
| Carry-Outs | _____ |
| General Merchandising Stores | _____ |
| Hardware | _____ |
| Hearing Aids | _____ |
| Home Furnishings/Furniture | _____ |
| Laundries, Dry Cleaning - Services | _____ |
| Maintenance/Cleaning/Sanitation - | _____ |
| Services/Supplies | _____ |
| Mobile Homes | _____ |
| Motels, Hotels | _____ |
| Paint and Decorating Supplies | _____ |
| Recreation/Entertainment/Travel - | _____ |
| Services/Supplies | _____ |
| Service Stations (Gasoline) | _____ |
| Signs | _____ |
| Vending | _____ |
| Water Conditioning | _____ |
| Miscellaneous Wholesale/Retail | _____ |
| and Service Businesses | _____ |

9. Please provide some details on the history of your franchise system:

(1) Number of outlets in operation at the end of the following years:

| | <u>1968</u> | <u>1969</u> | <u>1970</u> (est.) |
|--|-------------|-------------|--------------------|
|--|-------------|-------------|--------------------|

Franchised Outlets _____

Company Operated Outlets _____

(2) Date of sale of first franchise _____

Date of opening of first franchised outlet _____

Date of opening of first company-operated outlet _____

(3) For 1968, 1969 and 1970, please note the operating changes in these categories:

| | <u>1968</u> | <u>1969</u> | <u>1970</u> |
|--|-------------|-------------|-------------|
|--|-------------|-------------|-------------|

Discontinued or closed outlets _____

Company-operated outlets changed to franchised outlets _____

Franchised outlets repurchased and changed to company-operated outlets _____

Franchised outlets repurchased and sold to new franchisees (before or after terms expired) _____

Franchised outlets sold directly by franchisee to new franchisee _____

Franchised outlets where franchises terminated by franchisors and outlets reopened under new franchisees _____

Franchised outlets where franchises terminated by franchisees and outlets reopened under new franchisees _____

Franchisor Questionnaire

3.

10. The following questions are concerned with the representation of your franchise program to potential franchisees:

(1) Materials - please attach a representative sample of advertisements and promotional-informational materials presently used to instruct and inform potential franchisees.

(2) Do you require a deposit to be paid by a potential franchisee prior to his obtaining a copy of the franchise agreement? _____

(3) Do you show profit and loss statements of outlets already in operation to potential franchisees before they sign the agreements? _____

(4) Do you require a potential franchisee to obtain his own legal counsel? _____

(5) What prior business experience do you require of a franchisee?

(6) Do you normally select locations first and then offer them to potential franchisees? _____

(7) Has your company ever engaged an independent franchise sales agency? _____

At present? _____

(8) Did your company ever give "master" franchises that allow the franchisee to subfranchise to other people? _____

At present? _____

(9) What procedure is used to identify the territory or market allocated to a particular outlet?

(10) Please indicate the typical investment required of a new franchisee and the minimum cash that he will be required to put up for a franchise:

| | <u>Typical Investment</u> | <u>Minimum Cash Req'd.</u> |
|---|---------------------------|----------------------------|
| Land | \$ _____ | \$ _____ |
| Building | _____ | _____ |
| Sign(s) | _____ | _____ |
| Equipment | _____ | _____ |
| Initial Inventory | _____ | _____ |
| Franchise Fee | _____ | _____ |
| Deposit/Bond Fee to ensure proper performance by franchisee | _____ | _____ |

Franchisor Questionnaire

4.

10. (10) Cont'd.

Typical
Investment

Minimum
Cash Req'd.

Other - please specify

\$ _____

\$ _____

Total

\$ _____

\$ _____

(11) Please indicate the financing arrangements and terms available through you, the franchisor:

(12) Do you have an operating manual?

If yes, is it regarded as part of the franchisor agreement?

Is the operating manual made available to potential franchisees before they sign the agreements?

11. The Franchise Agreement and the Continuing Relationship Between the Franchisor and Franchisee:

(1) Training

(a) Do you provide formal training?

For how long (in weeks)?

(b) Do you provide on-the-job training?

For how long (in weeks)?

(c) Do you provide a supervisor to assist an opening franchisee?

For how long (in weeks)?

(d) Do you employ "field men" who regularly visit the franchisee?

Who pays for their expenses while visiting?

(2) Accounting and Record Keeping

(a) Do you require a standard bookkeeping system for your franchisees?

(b) At what intervals are the franchisee's records to be shown or made available to the franchisor?

(c) At what intervals are inventory checks required?

Franchisor Questionnaire

5.

11. (2) (c) Cont'd.

Who conducts these checks?

Franchisor _____
Franchisee _____
Outside Party _____

How is an inventory check conducted?
(check appropriate lines)

During business hours _____
Outside business hours _____
Franchisee must be present _____
Franchisee need not be present _____

In the event of an inventory shortage, what happens?
(check appropriate lines)

Franchisee must be notified immediately
on conclusion of check _____

Shortage referred to arbitration _____

Franchisee held responsible _____

Franchisee subject to loss of
deposit or bond (if any) _____

Franchise subject to termination _____

(3) Advertising

(a) Do your franchisees contribute to an
advertising fund? _____

If yes, on what basis? _____

(b) When and how are unused funds returned to the franchisees?

(c) Do you require approval of the advertising material used
by your franchisees? _____

(4) Purchasing, Pricing and Product Lines

(a) Do you require the franchisee to purchase operating supplies from you? _____

(b) Do you approve the major suppliers for the franchisee? _____

(c) Must the franchisee purchase equipment from you or an
affiliated company? _____

11. (4) Cont'd.

(d) Does the franchisee have minimum purchase requirements from you?

(e) Do you include a handling charge on supplies that you purchase and, without further processing, sell to a franchisee?

If yes, how much is charged and how is it computed? _____

(f) Do you charge a royalty? _____

If yes, what is the percentage and on what basis is it computed?

(g) Must the franchisee obtain your approval to add or delete to his product line?

(h) Do you specify the prices of the franchisee's products?

(i) Do you provide franchisees a list of suggested prices?

(j) Do you indicate the maximum prices the franchisee can charge?

12. Termination, Transfer and Renewal of the Franchise Agreement

(1) If a franchisee defaults on part of his contract, what time if given to him to rectify the situation?

(2) Is there an arbitration clause in the agreement governing relations here? Whom does it bind?

(3) Can a franchisee terminate the agreement by giving advance notice to you?

How many days' notice is required? _____

Is a fee charged to exercise this privilege? _____

(4) In what circumstances are you allowed to terminate the agreement?

How many days' notice is required? _____

Franchisor Questionnaire

7.

12. Cont'd.

(5) Is the term of the franchise normally the same as:

(a) Term of building lease? _____

If not, why not? _____

(b) Term of equipment agreement? _____

If not, why not? _____

(6) Upon Termination:

(a) Do the tangible assets of the franchise become your property? _____

(b) Are "security" deposits or other monies paid by the franchisee forfeited? _____

(c) Does "goodwill" enter into the accounting on behalf of the franchisee? _____

(d) Are parts of any fees returned? _____

(7) Upon expiration of the franchise agreement, is it renewable at franchisee's option? _____

If yes, for how many years? _____

If yes, how many times may he renew? _____

(8) If a franchisee renews a franchise agreement, does he pay a franchise renewal fee? _____

If yes, how much? \$ _____

(9) Upon the death of the franchisee, do his heirs inherit the rights to the franchise? _____

(10) Which of the following statements most accurately describes the rights of your franchisees to sell their franchises? Check One.

(a) Franchisee does not have any right to sell. _____

(b) Franchisee may only sell to us. _____

(c) We have "right of first refusal" and if not exercised, franchisee may sell to approved person. _____

(d) Franchisee may sell to anyone whom we approve. _____

(e) Franchisee may sell to any without our approval. _____

13. Do your franchisees have a franchisee organization? _____

If yes, what is the name and address? _____

13. Cont'd.

Are your franchisees allowed to join or form a franchisee organization?

14. Please enclose the following documents, if applicable:

- (a) Franchise agreement.
- (b) Operating manual for franchisees.
- (c) Building lease agreement.
- (d) Chattel mortgages.
- (e) Equipment agreement.
- (f) Any other agreements regarding insurance, training, etc.
- (g) List of names and addresses of your present franchisees.
- (h) Most recent annual report, if public company.

APPENDIX 10

THE DEPARTMENT OF FINANCIAL AND COMMERCIAL AFFAIRS

MINISTER'S COMMITTEE ON FRANCHISES

FRANCHISEE QUESTIONNAIRE

PLEASE COMPLETE AND RETURN BY JANUARY 31, 1971 TO:

Mrs. D. A. Stafl, Secretary
Minister's Committee on Franchises
Department of Financial & Commercial Affairs
555 Yonge Street
Toronto 284, Ontario

1. How do you conduct your business? Check one:

Sole Proprietorship _____
Partnership _____
Private Company _____

2. Please check the category which most appropriately describes your line of business.

| | |
|------------------------------------|-------|
| Automobile Dealers | _____ |
| Automotive Parts/Services | _____ |
| Auto/Trailer Rentals | _____ |
| Beauty Salons | _____ |
| Boats, Snow and Terrain Vehicles | _____ |
| Business Services/Equipment | _____ |
| Children's Stores | _____ |
| Clothing/Shoes | _____ |
| Construction/Remodeling - | _____ |
| Materials/Services | _____ |
| Cosmetics/Toiletries | _____ |
| Drug Stores | _____ |
| Educational Products/Services | _____ |
| Employment and Personnel Services | _____ |
| Entertainment/Recreational Centres | _____ |
| Equipment Rentals | _____ |
| Food - Convenience Stores | _____ |
| Food - Donuts, Pancakes, Waffles | _____ |
| Food - Ice Cream/Candy/Popcorn/ | _____ |
| Beverages | _____ |
| Food - Restaurant/Drive-Ins/ | _____ |
| Carry-Outs | _____ |
| General Merchandising Stores | _____ |
| Hardware | _____ |
| Hearing Aids | _____ |
| Home Furnishings/Furniture | _____ |
| Laundries, Dry Cleaning - Services | _____ |
| Maintenance/Cleaning/Sanitation - | _____ |
| Services/Supplies | _____ |
| Mobile Homes | _____ |
| Motels, Hotels | _____ |
| Paint and Decorating Supplies | _____ |
| Recreation/Entertainment/Travel - | _____ |
| Services/Supplies | _____ |
| Service Stations (Gasoline) | _____ |
| Signs | _____ |
| Vending | _____ |
| Water Conditioning | _____ |
| Miscellaneous Wholesale/Retail | _____ |
| and Service Businesses | _____ |

3. How many units do you operate? _____

4. Are you a "master" franchisee (i.e. you have subfranchisees under you)? Yes _____

No _____

Number of units you operate _____
Number of units operated by
subfranchisees _____

5. What type of work did you have before you bought your franchise?

6. How did you learn about the opportunity to buy a franchise?

7. Who sold you the franchise?

(1) Directly from franchisor _____

(2) Directly from another franchisee _____

(3) A "master" franchisee _____

(4) A franchise broker (someone who sells
several different franchises) _____

8. Please answer yes or not to the following:

(1) I consulted a lawyer before signing the
agreement. _____

(2) I consulted other advisor(s) before
signing the agreement. _____

(3) The franchisor suggested I seek
independent advice before signing
the agreement. _____

(4) I was shown profit and loss statements
for existing franchised units before
signing the agreement. _____

(5) I asked for and was given an opportunity
to study the agreement before signing
it. _____

(6) (If there was an operating manual) I
was given a similar opportunity to
study the manual before signing the
agreement. _____

(7) The agreement offered appeared to be
a standard form contract offered to
other franchisees. _____

(8) If yes to (5), it was possible to "dicker" over the terms and change the terms, at least in my case. _____

Give details:

9. Please indicate the investment that you had to get together to buy your franchise:

| | Total Outlay | Cash Required |
|--|--------------|---------------|
| Land | \$ _____ | \$ _____ |
| Building | _____ | _____ |
| Sign(s) | _____ | _____ |
| Equipment | _____ | _____ |
| Initial Inventory | _____ | _____ |
| Franchisee Fee | _____ | _____ |
| Security Deposit/Good Performance Fee (can be forfeited by franchisor) | _____ | _____ |
| Other - please specify | _____ | _____ |
| | _____ | _____ |
| | _____ | _____ |
| | _____ | _____ |
| | _____ | _____ |
| Total | \$ _____ | \$ _____ |

10. Who provided your financing, assuming that you required credit help? Check appropriate line(s) and indicate appropriate percentage of total financing.

| | | |
|--------------------|-------|-------|
| Bank | _____ | _____ |
| Franchisor | _____ | _____ |
| Friends, Family | _____ | _____ |
| Others | _____ | _____ |

11. Did you receive training when you bought your franchise?

For how long? (where) _____

Were you satisfied with it? _____

Was it included in your franchisee fee? _____

12. Are you required to maintain a standard accounting and bookkeeping system?

How frequently are your records to be available for study by the franchisor?

At what intervals are inventory checks required by the franchisor?

In the event of an inventory shortage, what happens?

Are you satisfied with the operation of this part of the franchise system? _____ If not, why not? _____

13. As between franchisor and franchisee, who decides the following?
Add comments if necessary.

(1) Prices of products or service. _____

(2) Additions to or deletions from product line. _____

(3) Sources of supply. _____

Franchisee Questionnaire

5.

13. (Con'd) (4) Hours of operation. _____

14. Which of the following statements most accurately describes your right to sell your franchise. (Please check one)

(1) I do not have the right to sell _____

(2) I may sell only to my franchisor _____

(3) I may sell to an approved person, subject to franchisor's "right of first refusal" to buy back the franchise. _____

(4) I may sell to anyone who is approved by my franchisor. _____

15. What apparently are the franchisor's sources of income from your operations (apart from initial investment, Question 9)?

e.g. - royalty, income from sales to you, advertising levy, etc.

16. Do you belong to a franchisee organization? If yes, what is its name and address?

What are your views on the advantages/disadvantages of a franchisee organization?

17. How satisfied are you with the profitability of your franchised business up to now?

Very satisfied _____

Satisfied _____

Neither satisfied nor dissatisfied _____

Dissatisfied _____

Very dissatisfied _____

18. How do your profits correspond with the estimates of the franchisor when you signed the agreement? Check one:

Greatly overestimated _____
Overestimated _____
Neither overestimated nor
underestimated _____
Underestimated _____
Greatly underestimated _____

19. Suppose there were no such thing as a franchised business, what would you be doing today? Check one:

(1) I would be self-employed in this same kind of business (but with no franchise). _____

(2) I would be self-employed in a different kind of business (but with no franchise). _____

(3) I would not be self-employed. _____

20. If you have the time, we would greatly appreciate your comments on the following points:

(1) My views on the promotion and advertisement of franchising opportunities by franchisors.

(2) My views on the form and content of franchise agreements and how they are interpreted during the life of the franchise.

20. (Cont'd)

(3) My views on the termination, transfer or removal of franchise requirements.

Thank you very much.



3 1761 11469336 9